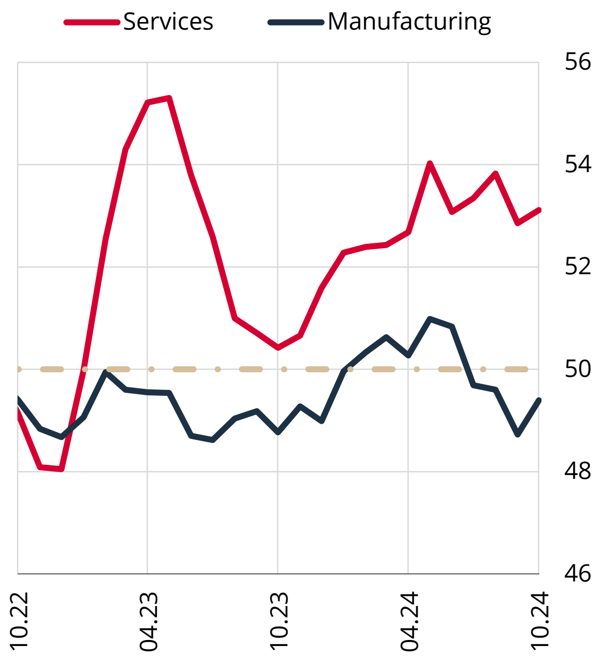
2. Economic Outlook

2.1 Global Economy

Leading indicators for global growth suggest that the weak course continues in the manufacturing industry, with the services sector remaining the main driver of economic growth. The global PMI for the manufacturing industry fell below the threshold value and remained weak. The services PMI recorded a decline over the previous reporting period, yet the index remained above the threshold value (Chart 2.1.1). The growth forecasts for Türkiye's trading partners vary according to their sensitivity to geopolitical developments as well as expectations regarding inflation and monetary policy. Compared to the previous reporting period, the change in growth outlook for 2024 for advanced economies was more favorable, while that for countries in Eastern Europe and the Middle East was negative (Table 2.1.1). The US exhibits a stronger growth outlook than other advanced economies. On the other hand, due to the relatively bad performance in the second quarter as well as the lower than expected broad-based monetary and fiscal expansion, China's growth forecast for 2024 was revised downwards. Moreover, China's annual growth receded to the lowest level of the last eighteen months in the third quarter. Against this background, the global growth index weighted by the export shares of Türkiye's trading partners is estimated to increase by 2.0% in 2024, remaining unchanged since the previous reporting period. On the other hand, the evident differences among countries were noteworthy, although the global growth expectation of 2.4% was preserved for 2025. These growth forecasts were revised downwards for the euro area and upwards for the US, UK and United Arab Emirates but remained unchanged for China. Joint evaluation of realizations, forecasts and leading indicators reveals that downside risks to the global growth outlook have accumulated overall since the release of the previous Inflation Report.

Chart 2.1.1: Global PMI Indices (Level)



Source: S&P Global.

Table 2.1.1: Growth Forecasts for Türkiye's Main Trading Partners* (%)

	2023	2024 Forecast		2025 Forecast	
		IR 2024-III	IR 2024-IV	IR 2024-III	IR 2024-IV
Euro Area	0.4	0.7	0.7	1.4	1.2
Germany	-0.3	0.2	0.0	1.1	0.7
USA	2.9	2.3	2.6	1.7	1.8
UK	0.3	0.8	1.0	1.1	1.3
Italy	0.7	0.9	0.8	1.0	0.9
Iraq	-0.6	1.1	0.7	2.1	2.0
Spain	2.5	2.3	2.7	1.9	2.0
France	1.1	0.9	1.1	1.2	1.0
Netherlands	0.1	0.4	0.6	1.4	1.4
Israel	2.0	1.5	1.0	3.9	3.5
Russia	3.6	3.2	3.5	1.7	1.6
UAE	2.9	3.4	4.0	2.1	5.7
Romania	2.1	2.8	2.0	3.5	3.1
Belgium	1.4	1.2	1.2	1.5	1.3
Poland	0.2	2.9	3.1	3.8	3.7
Egypt	3.8	3.4	2.9	4.2	4.1
Bulgaria	1.8	2.2	2.2	2.9	2.9
China	5.2	4.9	4.8	4.4	4.4

Source: Consensus Economics, S&P Global.
* Countries are ranked according to the size of their share in Türkiye's exports in 2021.

The global growth outlook and composition, geopolitical risks, financial conditions, and supply-side factors continue to play a determining role in commodity prices. Having trended downwards in summer, non-energy commodity prices showed widespread increases compared to the previous reporting period. Meanwhile, the volatility in oil prices was noteworthy. The persisting political tensions in Russia-Ukraine and the Middle East as well as the decisions of the OPEC+ member countries to cut output cause sustained upside pressures in oil prices, while the languid course of demand leads downside pressures to persist.

Natural gas prices also show fluctuations amid the geopolitical turmoil. However, due to the euro area growth outlook, mild weather conditions and the increase in the imports of liquefied natural gas, natural gas stock levels remained high and had a downward effect on prices that are indicative for Europe. Thus, natural gas prices fell by 2.8% over the previous reporting period. Meanwhile, amid China's incentives launched to allay deflation concerns and achieve its growth target, industrial commodity prices have surged since the release of the previous Inflation Report. Agricultural commodity prices also rose noticeably compared to the previous reporting period due to climatic conditions (Table 2.1.2).

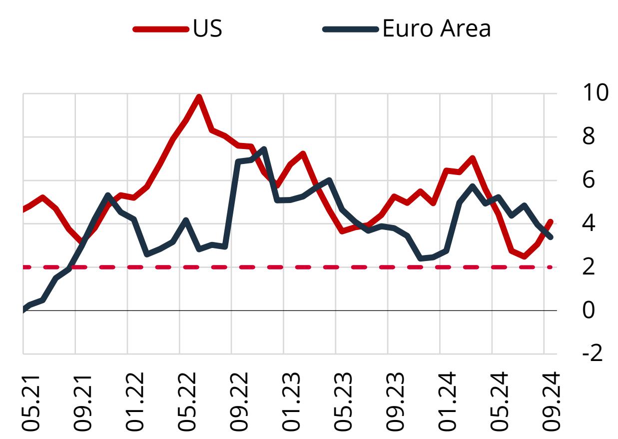
Table 2.1.2: Commodity Prices (%)

	July 2024	August 2024	September 2024	October 2024	Annual	Compared to the Previous Reporting Period*
Headline Commodity Index	-1.4	-4.8	-2.6	3.5	-7.5	-0.9
Energy	0.4	-6.6	-6.9	3.8	-16.5	-7.0
Agricultural Commodity	-7.0	-3.1	5.1	1.2	-7.6	4.5
Industrial Metal	-3.8	-2.5	2.9	4.3	16.3	10.5
Precious Metal	3.4	2.5	3.7	4.5	40.7	12.1
Excl. Energy	-3.7	-2.3	3.2	3.0	6.5	7.6
Brent Oil	3.3	-5.2	-8.1	1.8	-16.9	-8.0
Natural Gas (USA)	-21.2	-6.0	14.9	7.6	-18.2	25.2
Natural Gas (Europe)	-5.6	18.0	-5.7	11.4	-14.1	-2.8
Coal	1.1	7.8	-3.9	3.8	4.2	-1.1
Aluminum	-5.8	0.1	4.5	5.6	18.4	15.8
Copper	-3.0	-5.9	3.1	4.5	22.7	10.4
Iron	1.2	-8.3	-6.8	14.1	-10.6	2.2
Wheat	-9.0	-3.1	7.8	2.9	2.2	5.7
Soy	-4.6	-12.0	2.8	-1.0	-21.9	-2.7
Rice	-11.3	-5.8	2.1	-1.5	-5.6	-1.1
Corn	-9.4	-5.5	6.1	4.2	-14.8	9.3
Cotton	-4.4	-1.0	4.1	1.2	-15.5	6.7
Sugar	1.0	-4.8	12.0	8.4	-16.9	18.8

Source: Bloomberg.
* Denotes percentage change in prices between November 1, 2024 and August 8, 2024.

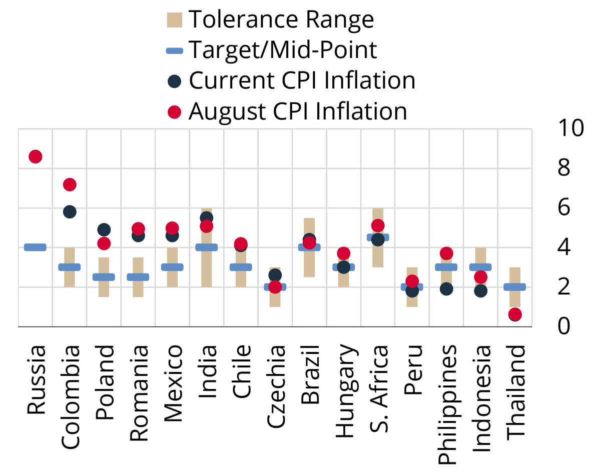
As global disinflation continues, the stickiness in service inflation declines, yet it is still in place. Geopolitical developments and fluctuations in commodity prices continue to pose a risk to the disinflation process, while the mild course in supply conditions and the tight monetary policy stance further support the decline in inflation at a global scale. It is noteworthy that wage pressures weakened as the supply and demand balance in labor markets continued to normalize and price increases in the services sector were more moderate compared to the previous reporting period (Zoom-in 2.1). The data for the last two months showed that the underlying trend of US services inflation increased slightly and moved away from the target-consistent levels that it had been approaching. However, being attributed to the one-off increases in health and transportation services in September, this did not cause a significant deterioration in the overall inflation outlook and inflation expectations in the US. In the euro area, price increases in services tumbled further (Chart 2.1.2). Meanwhile, although inflation remained outside the tolerance range in some Eastern European and Latin American countries, and annual inflation edged up in some countries, in general, inflation rates in emerging economies converged more to the targets compared to the previous reporting period (Chart 2.1.3).

Chart 2.1.2: Services Inflation in Advanced Economies (Annualized Three-Month Moving Average, Seasonally Adjusted, %)



Source: ECB, St Louis Fed.

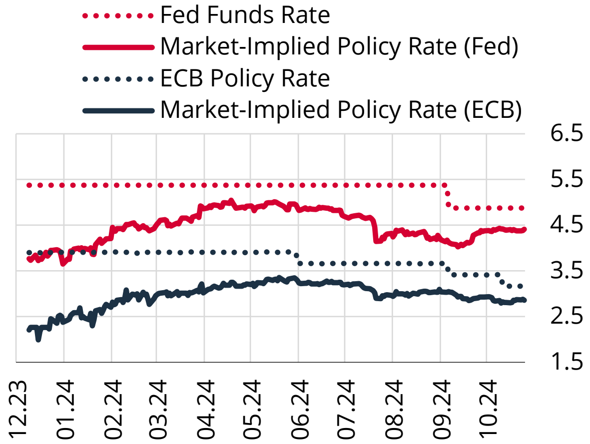
Chart 2.1.3: Consumer Inflation in Emerging Economies (Target, Tolerance Range and Realization, %)



Source: Bloomberg.

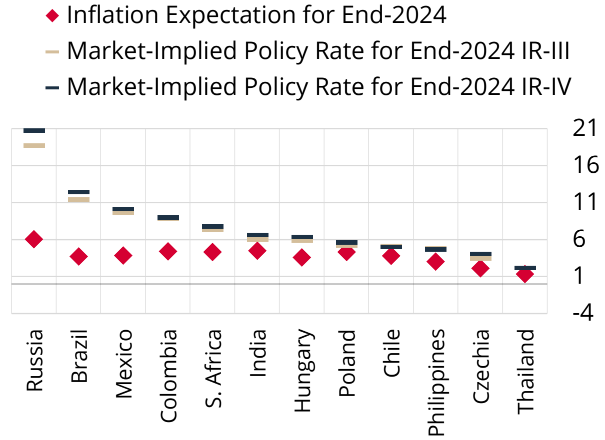
As inflation declines further, major central banks opt for rate cut cycles and market pricings suggest that rate cuts will continue. The Fed initiated the policy rate cut process in its September meeting with 50 basis points. Meanwhile, median expectations of the Fed members were revised in a way to indicate further rate cuts for 2024 and 2025 compared to July (Box 2.1). The communication signaled that, depending on the data, rate cuts may continue in the upcoming meetings of the year. The recent strong course of the labor market reinforced expectations that the stance for the rate cuts would be more cautious. The European Central Bank (ECB), on the other hand, continued to cut rates by 25 basis points at its October meeting and signaled that it may opt for further reductions until the end of the year depending on inflation and economic activity dynamics. As a result, as of November 6, the amount of additional rate cuts priced until the end of the year is 46 basis points for the Fed and 30 basis points for the ECB (Chart 2.1.4). In the current reporting period, the Bank of Canada and Danmarks Nationalbank cut their policy rates by 25 basis points each and the Bank of Sweden by 50 basis points, while the central banks of South Korea (25 basis points) and New Zealand (75 basis points in two meetings) took first steps towards easing. On the other hand, the Bank of Japan, which raised its policy rate by 15 basis points in July, communicated that it would implement additional rate hikes over a wider period of time. Meanwhile, emerging economies maintained their cautious stance in their interest rate cuts due to the slowing improvement in the inflation outlook. In the current reporting period, the Bank Indonesia, the South African Reserve Bank, the National Bank of Romania and the Bank of Thailand initiated rate cuts by 25 basis points each and the Central Bank of Philippines by 50 basis points in two meetings, while the Central Reserve Bank of Peru (50 basis points), Banco de Mexico (50 basis points), Central Bank of Colombia (100 basis points), the Czech National Bank (25 basis points), the Central Bank of Chile (50 basis points) and Magyar Nemzeti Bank (25 basis points) continued to cut policy rates. Having revised its inflation forecasts upwards, the Banco Central do Brasil opted for a raise in policy rates by 25 basis points, while the Bank of Russia continued to increase rates by 300 basis points. China, on the other hand, announced accommodative monetary and fiscal decisions to alleviate concerns over deflation and achieve its 5% growth target. In the coming period, rate cuts are likely to continue in advanced and emerging economies in line with the fall in inflation. However, considering the levels of inflation, rigidities and the recent elevation in the Middle East-related geopolitical risks, it is expected that the rate cuts will be delivered in a way that maintains monetary tightness and sustains the disinflation process. Compared to the previous reporting period, many emerging economies are pricing in slightly higher interest rates for end-2024. Moreover, policy rates implied by futures and inflation expectations suggest that interest rates in emerging economies will continue to be set above inflation rates (Chart 2.1.5).

Chart 2.1.4: Market-Implied Policy Rate for End-2024 (Effective, %)



Source: Bloomberg.

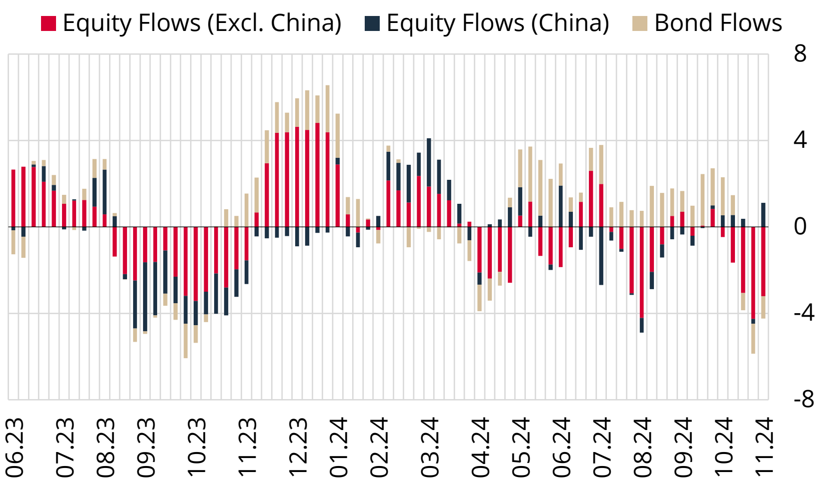
Chart 2.1.5: Futures-Implied Policy Rate and Inflation Expectations* (% Points)



Source: Bloomberg.
* Inflation expectations are from the Bloomberg Survey. Policy rate pricings are calculated in view of six-month-forward contracts for IR 2024-III and three-month-forward contracts for IR 2024-IV.

Fluctuations in the global risk appetite and uncertainties regarding the policy decisions of major central banks have led to a volatile course in portfolio inflows to emerging economies. Volatilities in pricing of rate cuts by major central banks and global uncertainties during the previous reporting period had a negative effect on the risk perceptions towards emerging economies. This caused fluctuations in portfolio flows to continue into the current reporting period. Moreover, the divergence in portfolio flows towards equity and bond-bill markets seen in previous periods continued in the current reporting period. Between August 8 and November 1, outflows from equity markets excluding China amounted to USD 6.7 billion, while outflows from debt securities markets remained limited to USD 250 million (Chart 2.1.6). In the upcoming period, policy decisions of major central banks, developments in the Chinese economy and geopolitical developments in the Middle East are expected to shape portfolio flows to emerging economies.

Chart 2.1.6: Weekly Portfolio Flows to Emerging Economies
(Four-Week Moving Average, USD Billion)



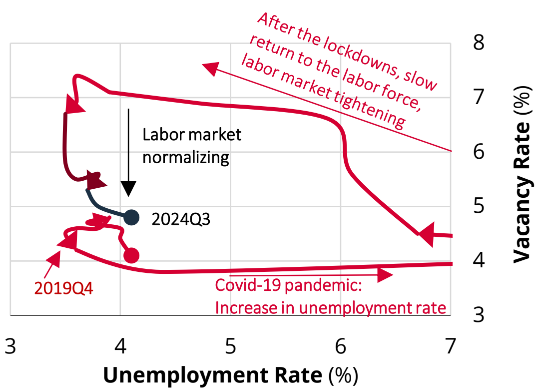
Source: IIF.

Zoom-in 2.1

Normalization in the US and Euro Area Labor Markets

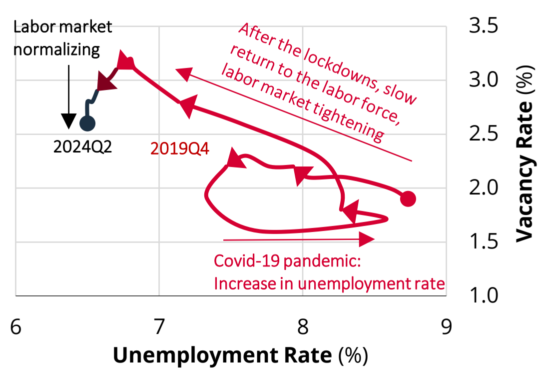
Unemployment rates increased in the US and the euro area after the lockdowns during the pandemic, but labor markets tightened due to the decline in the number of job seekers in the subsequent recovery period. While production resumed, the return to the labor force proved rather slow, both due to the need for childcare amid longer closure of schools and the fear of getting infected. In advanced economies, the decline in the number of workers migrating from abroad, the increase in early retirements due to the pandemic and increased savings during the shutdown period also had a reducing impact on labor force participation rates. In the meantime, while the rate of job vacancies increased rapidly, the number of job seekers did not rebound equivalently and a notable demand surplus emerged in labor markets. The process was similar in the US and the euro area, with labor market tightness peaking in late 2022 (Charts 1 and 2). The excess demand in labor markets put upside pressure on wages and, together with the buoyant demand in the services sector, was a significant factor that slowed down the disinflation process.

Chart 1: US Beveridge Curve*



Source: U.S. Bureau of Labor Statistics.

Chart 2: Euro Area Beveridge Curve*



Source: Eurostat.

* The Beveridge Curve with the vacancy rate on the vertical axis and the unemployment rate on the horizontal axis shows the degree of tightness in the labor market. As the vacancy rate increases and the unemployment rate decreases or as the trend moves up and to the left in the chart, the supply-demand balance shifts in favor of demand and the labor market tightens. As the trend moves down and to the right, the balance shifts in favor of supply and the upward pressure on wages weakens.

Recently, supply and demand in the labor market have appeared to be more balanced.

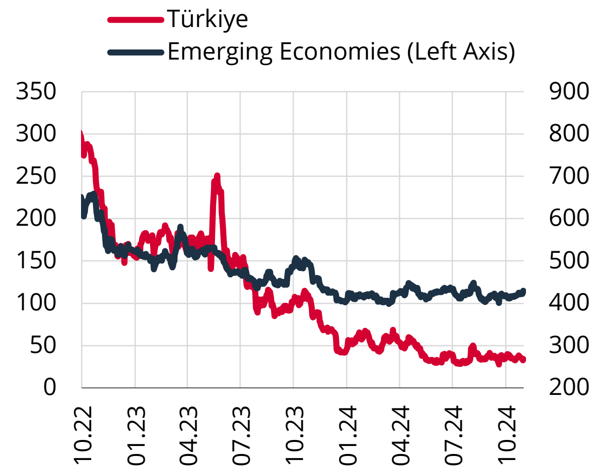
Supply constraints and supply setbacks in the goods market following the pandemic have waned mostly after China's easing of pandemic measures, but the contraction in labor supply has been more persistent. On the other hand, along with the lagged effects of the monetary policy, a normalization and cooling trend in labor markets has been noted recently. This trend is much more evident in the US, where the job openings-unemployment balance has approached pre-pandemic levels (Chart 1). Meanwhile, in the euro area, despite the normalization trend, the job vacancy rate is still higher and the unemployment rate is lower than the pre-pandemic period (Chart 2). However, there is also empirical evidence that the natural rate of unemployment for the euro area has also settled on a downtrend and that current unemployment levels are not far below the long-run equilibrium.[1] In sum, the labor market normalization continues in advanced economies and the stickiness in services prices continues, albeit at a weaker pace.

[1] Růžičková, P. (2024). Unemployment in the Euro Area: Why Is It So Low and When Will It Start to Rise? Czech National Bank Blog.

2.2 Financial Conditions

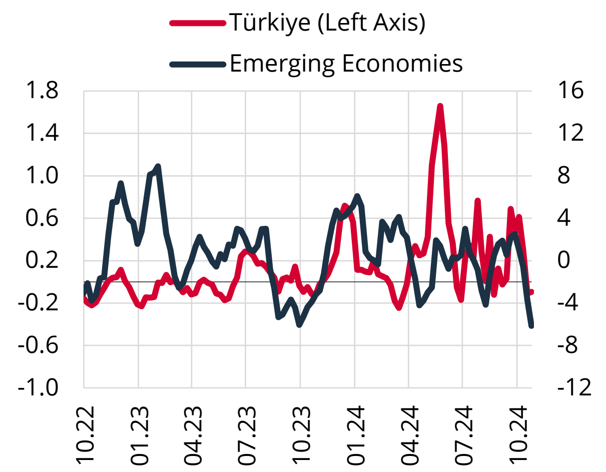
Global risk appetite, which deteriorated sharply in early August due to geopolitical developments, recession concerns and the Bank of Japan's surprise rate hike, improved thereafter, but the recovery remained limited amid geopolitical risks and uncertainties over the US elections. The Fed's decision to cut rates, joining other major central banks that have started to lower interest rates, has boosted the recovery in global risk appetite. However, rising tensions in the Middle East and uncertainty over the US elections continued to be the main risk factors for global financial conditions. Against this backdrop, emerging market risk premiums fell to their pre-August levels, and in parallel, Türkiye's CDS premium dropped to 272 basis points as of October 25 (Chart 2.2.1). The volatility in risk appetite during the current reporting period resulted in outflows from emerging market assets, while portfolio inflows to Türkiye totaled USD 1.88 billion, comprising net inflows of USD 3.23 billion to the government domestic debt securities (GDDS) market and net outflows of USD 1.35 billion from the equity market (Chart 2.2.2).

Chart 2.2.1: CDS Premium in Türkiye and Emerging Economies* (Five-Year, Basis Points)



Source: Bloomberg.
* Emerging economies include Brazil, Chile, Colombia, Indonesia, Malaysia, Mexico, South Africa and the Philippines.

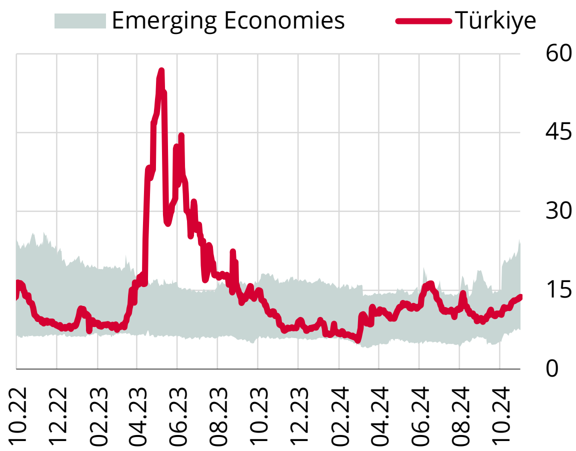
Chart 2.2.2: Portfolio Flows to Türkiye and Emerging Economies* (Four-Week Average, USD Billion)



Source: CBRT, IIF.
* Data for Türkiye includes portfolio flows to equity and GDDS markets. Repo is excluded from the GDDS data.

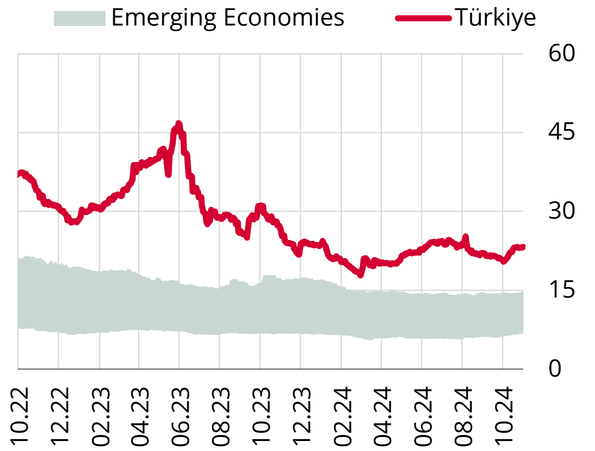
The implied volatility of the Turkish lira has recently increased. Exchange rate volatilities, which trended sharply upwards due to the short-lived turbulence in global markets in early August, declined in the following period in line with the improvement in global risk sentiment. Meanwhile, the higher-than-expected inflation in September exerted downward pressure on TL-denominated asset prices and increased the volatility of the Turkish lira in both the short and long term. Following the recent increase, the one-month implied exchange rate volatility of the Turkish lira has risen to 13.7%, while the 12-month volatility stood at 23.2% (Charts 2.2.3 and 2.2.4). The difference between short- and long-term volatilities indicates that policies continue to have an impact on exchange rate stability, yet longer-term risks persist.

Chart 2.2.3: Implied Volatility of FX Options*
(Against USD, One-Month Maturity, %)



Source: Bloomberg.
* Emerging economies include Brazil, Chile, Colombia, Mexico, Poland, the Philippines, Malaysia, South Africa, Indonesia, Romania and Hungary.

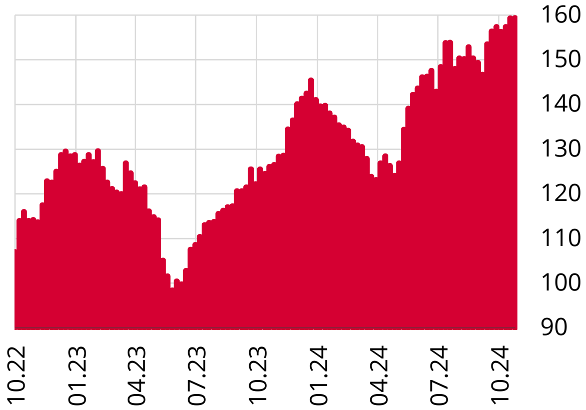
Chart 2.2.4: Implied Volatility of FX Options*
(Against USD, One-Month Maturity, %)



Source: Bloomberg.
* Emerging economies include Brazil, Chile, Colombia, Mexico, Poland, the Philippines, Malaysia, South Africa, Indonesia, Romania and Hungary.

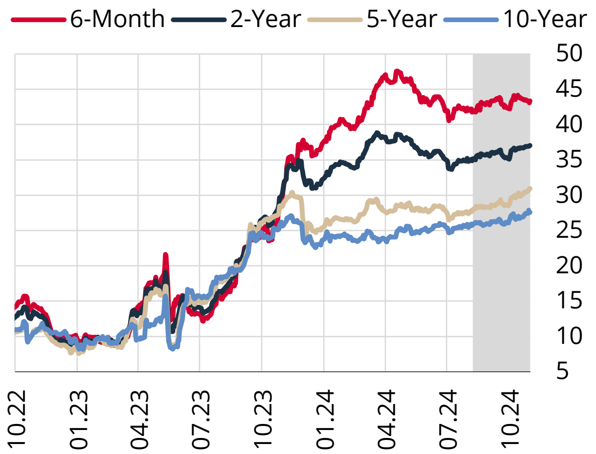
The strong upward trend in CBRT reserves continues. Maintaining their upward trend, the CBRT's gross international reserves reached USD 159.4 billion as of October 25 (Chart 2.2.5). The increase in reserves is a reflection of the ongoing interest of residents and non-residents in TL-denominated assets. Moreover, while Turkish lira funding via swap operations was zeroed out as of the previous reporting period, the CBRT started Turkish lira currency swap transactions in order to diversify the sterilization instruments. As of October 25, when these transactions, which amounted to USD 4.57 billion, are included, the total reserves reached USD 164 billion.

Chart 2.2.5: CBRT's Gross International Reserves (Weekly, USD Billion)



Source: CBRT.

Chart 2.2.6: GDDS Yields (%)

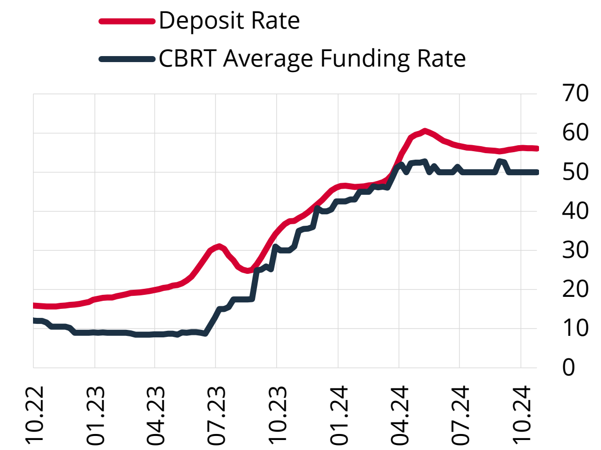


Source: Bloomberg.

GDDS yields have posted an increase. The September inflation realization led to an increase in GDDS yields, which was more prominent in short maturities (Chart 2.2.6). Despite the sustained interest of foreign investors in the GDDS market, supply-side factors are also influencing the long-term GDDS yields. As the disinflation process continues, and there is greater evidence of budget discipline, interest in the GDDS market is expected to grow further, and bond yields are expected to decline.

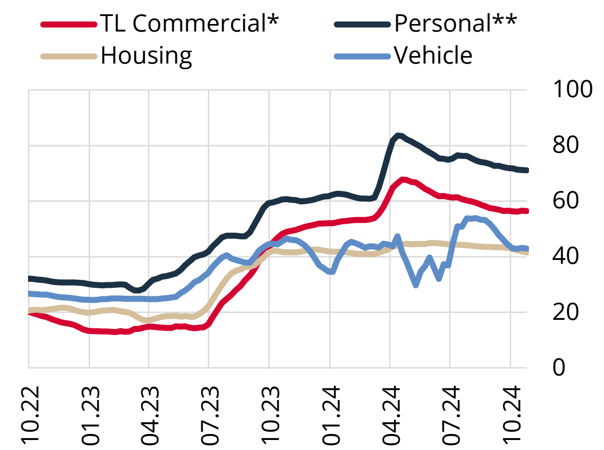
Tightness in financial conditions is maintained. During the current reporting period, the decline in inflation expectations for end-2024 has been slower than projected, while exchange rate expectations have shown a notable improvement. The decline in deposit rates observed during the second quarter of 2024 has been limited by the maintenance of the tight monetary policy stance, the effective sterilization of excess Turkish lira liquidity in the market through various instruments and the implementation of macroprudential measures to support Turkish lira deposits. In the current reporting period, Turkish lira deposit rates remained flat and stood at 55.8% as of October 25 (Chart 2.2.7). In order to support Turkish lira deposits, the CBRT took the following steps on August 29, 2024: The ratio for maintaining Turkish lira required reserves in blocked accounts has been increased by 5 percentage points, the monthly growth target has been increased for banks with real person Turkish lira deposit shares between 45% and 50%, the monthly growth target has been abolished for banks with real person Turkish lira deposit shares exceeding 60%, the condition to keep this share above 60% was introduced, and the upper limit for the remuneration of required reserves, which should be maintained for Turkish lira deposits, based on the rate of transition to Turkish lira has been increased from 80% to 84% of the policy rate. In addition, on September 21, 2024, reserve requirement ratios for Turkish lira deposits were raised in order to absorb excess Turkish lira liquidity in the market, and the transition-to-TL ratio condition for the remuneration of required reserves that should be maintained for Turkish lira deposits has been abolished in order to reduce the cost of required reserves to banks. Thus, the remuneration rate for required reserves that should be maintained for Turkish lira, which previously varied between 10% and 42% depending on the transition-to-TL ratio, has been raised to 42% for all banks. Furthermore, the maximum commission rate of 5% applied based on the level of transition-to-TL ratio has been raised to 8% to ensure that banks continue to meet their transition-to-TL ratio targets. Despite the flat course of Turkish lira deposit rates, Turkish lira commercial loan and personal loan rates have continued to decline since the second quarter of 2024. However, with the onset of the disinflation process in June 2024, real Turkish lira commercial loan and personal loan rates have moved into positive territory according to both expected and realized inflation, and the tightness in financial conditions became more evident. The decline in loan rates is attributed to banks' motivation to stimulate loan demand, which was weak and below growth limits, and their desire to support their profitability by extending loans at high interest rates before the start of policy rate cuts. As of October 25, Turkish lira commercial loan and personal loan rates dropped to 56.7% and 70.4%, respectively. Housing loan rates, which were relatively flat due to their long-term maturities, and vehicle loan rates, which fluctuate depending on the sales campaigns, were 41.3% and 41.7%, respectively, as of October 25 (Chart 2.2.8). With the press release of the Banking Regulation and Supervision Agency (BRSA) on September 20, 2024, the previously more prudently set risk weights for retail loans have been reduced to Basel standards, which may have a downward impact on retail loan rates in the coming period by reducing the regulatory burden on banks.

Chart 2.2.7: Turkish Lira Funding Rates* (Four-Week Moving Average, %)



Source: CBRT.
* Deposit rate is compound interest rate, while CBRT average funding rate is simple interest rate.

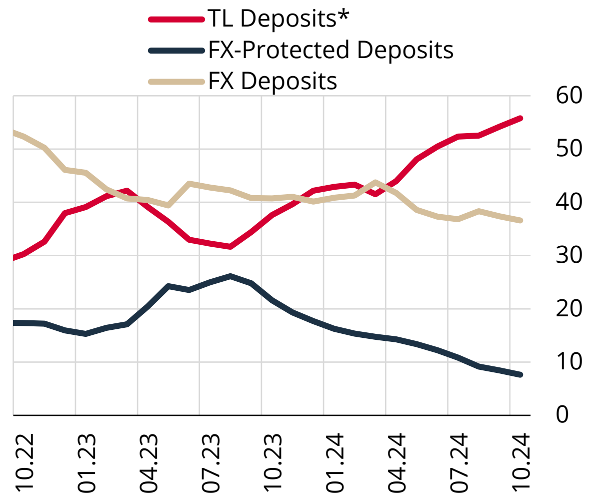
Chart 2.2.8: Loan Rates (Flow, Four-Week Moving Average, %)



Source: CBRT.
* Excluding overdraft accounts and credit cards.
** Excluding overdraft accounts.

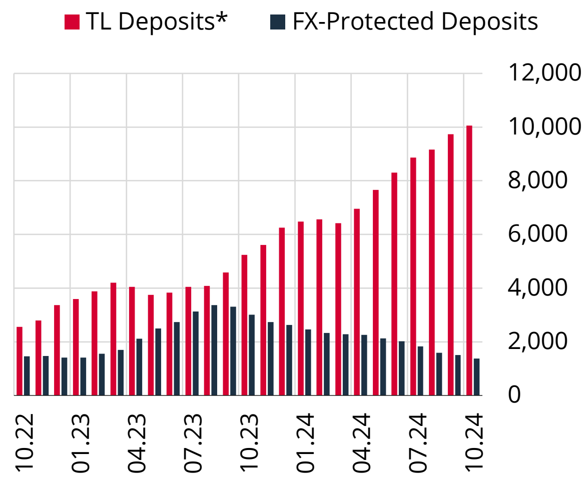
The share of Turkish lira in banks' deposit composition has continued to increase. The gains in the disinflation process and the macroprudential regulations supporting Turkish lira deposits led to a significant increase in the share of Turkish lira deposits, thereby exceeding the 50% target set for 2024. The Turkish lira share in banks' deposit composition increased by 3.4 percentage points to 55.8% in the current reporting period. The share of KKM in total deposits continued to decline as well, falling to 7.6% (Charts 2.2.9 and 2.2.10). In addition to the tight monetary policy, the policies aimed at increasing the share of Turkish lira deposits and encouraging transition from KKM accounts to Turkish lira deposits have also contributed to the increase in the share of Turkish lira deposits and the decline in the share of KKM accounts in the deposit composition. Despite a slight shift towards FX deposits in August due to volatility in global markets, this trajectory reversed in the following months. During this period, a number of decisions were taken concerning the KKM accounts. Following the CBRT's press release of August 29, 2024, legal person KKM accounts have been included again in the calculation of the total target for KKM accounts' transition to Turkish lira and renewals. Additionally, on September 2, 2024, the opening date for FX deposit accounts and precious metal accounts of real persons at banks was extended from March 31, 2024 to August 31, 2024 in order for real and legal persons to open KKM accounts. As a result of these decisions, the share of FX deposits started to decline again after August.

Chart 2.2.9: Deposit Composition (% Share)



Source: CBRT.
* TL deposits exclude KKM and FX-protected deposit accounts converted from FX (DDM).

Chart 2.2.10: Turkish Lira Deposit Composition (TRY Billion)

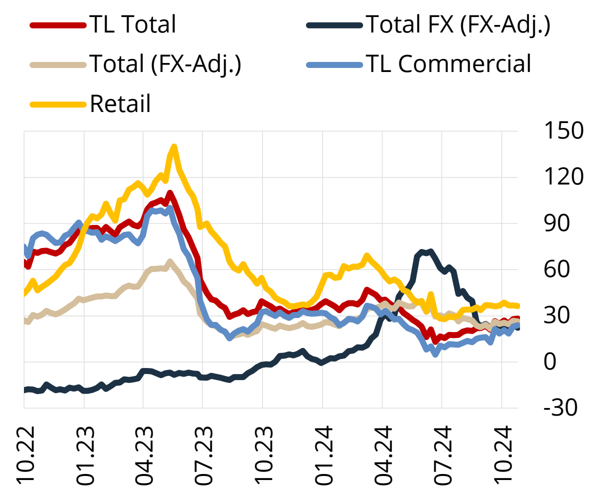


Source: CBRT.
* Data for Turkish lira deposits excludes KKM and DDM.

Tight financial conditions and macroprudential policies remain determinants of loan growth. The 13-week annualized growth rate of exchange rate-adjusted FX loans declined significantly to 22.2% as of October 25, after the 2% growth limit for FX loans introduced in May 2024 was reduced to 1.5% in July. Due to the growth limits for FX loans and declining Turkish lira commercial loan rates, firms' tendency to use Turkish lira commercial loans strengthened in the current reporting period, and the 13-week annualized growth rate of Turkish lira commercial loans rose to 23.9%. However, due to tight financial conditions and loan growth limits, the exchange rate-adjusted 13-week annualized growth rate of total commercial loans decreased to 23.5% in the current reporting period (Chart 2.2.11). While there are loans that are exempted from loan growth limits, total Turkish lira commercial loans, including exempted loans, and exchange rate-adjusted total FX commercial loans have been growing at a pace that is close to the path implied by the 2% and the 1.5% limits, respectively, thus contributing to the rebalancing in domestic demand. In order to support exporters' access to finance, the daily limit of TRY 3 billion for rediscount credits was raised to TRY 4 billion in October. Moreover, as of January 13, 2025, the exporter scores of firms calculated by considering variables such as the diversity of exported products and export destinations, the technological level of exported products and the scale of firms will be taken into account in credit extensions, in addition to being a net exporter. In light of these changes, Turkish lira commercial loan growth may see a slight uptick in the coming period. In the current reporting period, the 13-week annualized growth in retail loans rose to 36.3% as of October 25, driven by the growth in personal credit cards and housing loans, which were exempted from loan growth limits. Personal credit cards and housing loans grew by 41.6% and 28.3%, respectively.

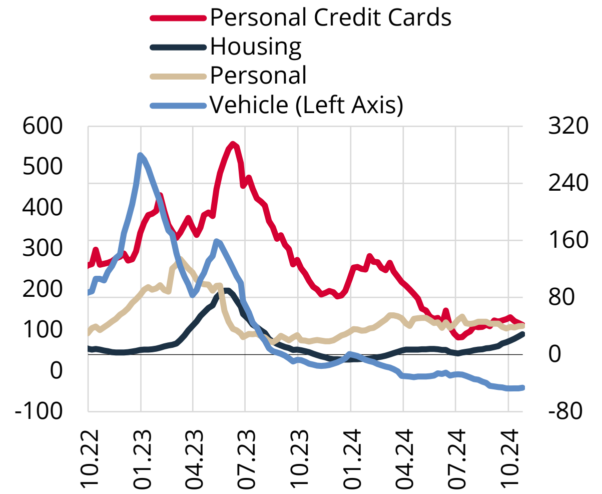
The increase in housing loan growth in the current reporting period is attributed to the rise in households' demand for housing loans due to the decline in the house price/rent ratio and banks' interest in utilizing their excess Turkish lira liquidity by extending long-term loans. Despite having accelerated slightly, the growth of housing loans remains similar to that of other loan types subject to limits, and the share of mortgage sales in total housing sales remains subdued at 11.2% as of September 2024. As for personal credit cards, their increased payment function since the pandemic and the installment facility they offer as an alternative borrowing option to personal loans, which are subject to growth limits, have been determinant in their growth. On September 27, 2024, the CBRT differentiated the maximum contractual interest rates for credit cards based on the amount of term debt of credit cards and raised the monthly interest rates for those with term debt exceeding TRY 150,000 from 4.25% to 4.75%, based on the current reference rate. The income elasticity of personal credit cards has declined in recent quarters, except for the high-balance group (Box 2.2). Increasing the maximum contractual interest rates of this group, which has a significant share in the personal credit card growth, may contribute to disinflation by reducing the personal credit card growth in the upcoming period. The 13-week annualized growth rate of personal loans declined slightly during the current reporting period to 40.4% as of October 25. While the growth in personal loans excluding overdraft accounts remained below the 2% growth limit, overdraft accounts had a significant impact on personal loan growth. The share of overdraft accounts in personal loans increased from 24.9% to 28.1% in the current reporting period. The 13-week annualized growth of vehicle loans has remained in the negative territory since March (Chart 2.2.12). On September 26, 2024, the BRSA announced a restructuring opportunity up to 60 months for personal credit cards with unpaid minimum due payments and personal loans with principal and/or interest payments more than 30 days overdue. This decision is expected to support banks' retail loan asset quality outlook and may have an upward impact on retail loan growth by increasing the performing loan balance.

Chart 2.2.11: Loan Growth (13-Week Annualized, FX-Adjusted, %)



Source: CBRT.

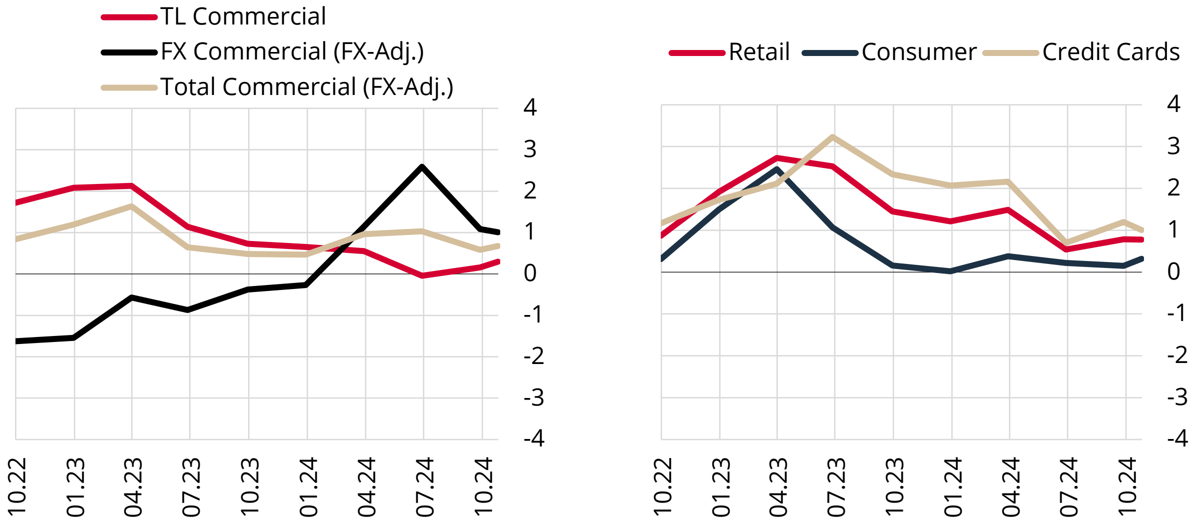
Chart 2.2.12: Retail Loan Growth (13-Week Annualized, %)



Source: CBRT.

Real credit utilization converged to long-term averages in FX-adjusted total commercial loans but remained above long-term averages in retail loans. With the impact of the loan growth limits introduced in May and tightened in July, exchange rate-adjusted FX commercial loan changes in real and standardized terms have started to decline, yet they are still above long-term averages. During the current reporting period, there has been a slight increase in the real Turkish lira commercial loan changes, yet they have remained close to long-term averages. With the impact of FX commercial loans, FX-adjusted total commercial loan changes in real and standardized terms declined but remained above long-term averages. Consumer loan changes in real and standardized terms are close to long-term averages due to relatively weak growth in vehicle and housing loans as well as personal loans subject to loan growth limits. Despite hovering above its long-term average, personal credit card rate changes in real and standardized terms, which were on a downtrend since the introduction of tight monetary policy, increased slightly again in the third quarter of 2024 (Chart 2.2.13).

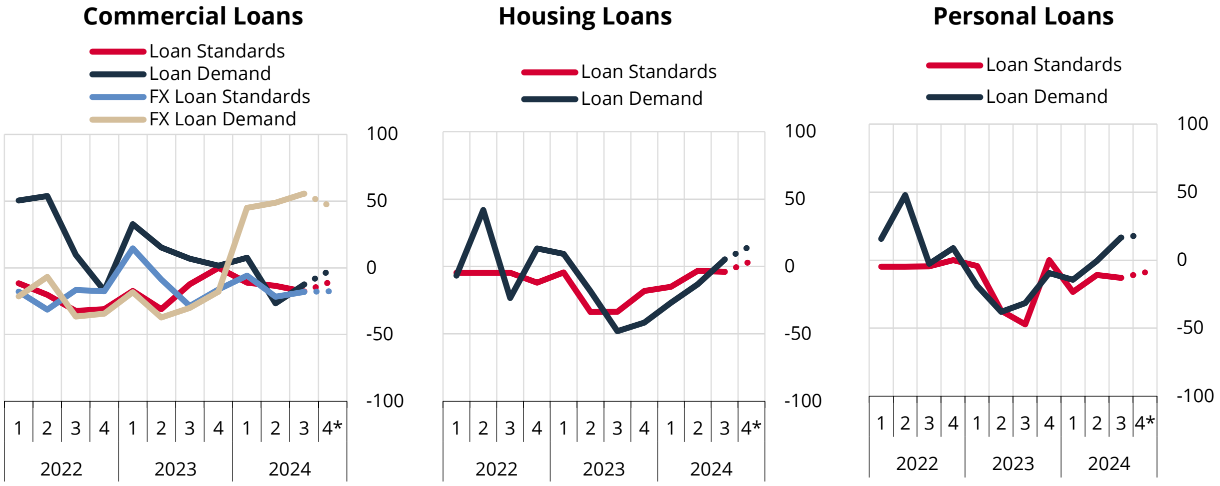
Chart 2.2.13: Credit Change* (13-Week Average, Real, Standardized Value)



Source: CBRT.
* Series are deflated by CPI. The mean and standard deviations of the series are calculated based on the 2006-2019 period. The 13-week average is taken after real weekly changes in loan stock balances are standardized. Consumer loans are composed of housing, vehicle and personal loans, while retail loans are the sum of consumer loans and personal credit cards.

According to the Bank Loans Tendency Survey (BLTS), loan standards excluding housing loans will remain tight in the last quarter of 2024. The fact that banks' loan standards for both personal and commercial loans were tight in the third quarter of 2024 has contributed to loan growth remaining below the limits. FX commercial loan demand has been strong since the first quarter of 2024 due to the lower cost implied by FX loan rates and exchange rate depreciation expectations compared to Turkish lira commercial loan rates. This outlook is expected to continue in the last quarter of 2024, albeit at a slightly weaker pace. On the other hand, the weak course in Turkish lira commercial loan demand that started in the second quarter of 2024 is projected to continue in the last quarter. Demand for personal and housing loans picked up in the third quarter of 2024 and is expected to continue to do so in the last quarter. The easing in only housing loan standards of banks and the increase in housing loan demand in the last quarter of 2024 are consistent with the recent increase in housing loan growth (Chart 2.2.14).

Chart 2.2.14: Loan Standards and Loan Demand*



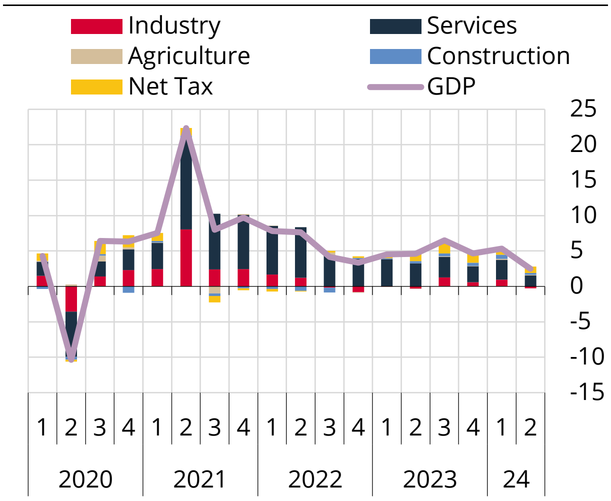
Source: CBRT BLTS.
* Denotes banks' expectations. Loan standards and loan demand are calculated as follows: Banks are asked how their loan standards (loan demand) have changed in the past three months. Net trends, which are calculated using percentages of responses, show the direction of change in loan standards (loan demand). An index above zero indicates easing in loan standards (increase in loan demand).

2.3 Economic Activity

Supply and Demand Developments

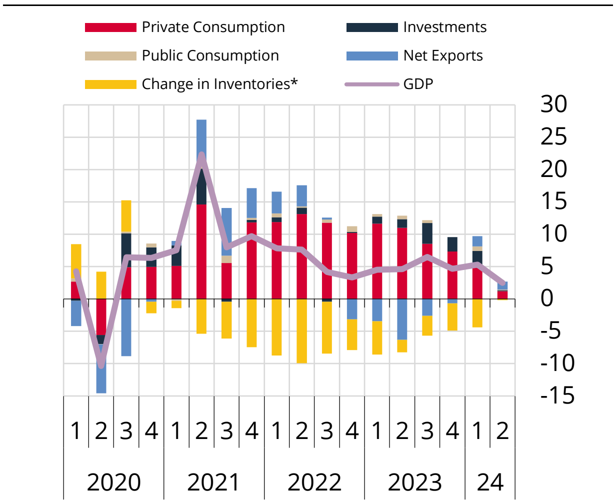
Annual and quarterly growth rates declined in the second quarter. In this period, GDP increased by 2.5% on an annual basis but remained flat on a quarterly basis with a growth of 0.1%. The fall in annual and quarterly growth rates indicated a weakening in economic activity compared to the first quarter. The services sector remained the main driver of annual growth on the production side. While the value added of the construction sector and net tax revenues continued to support growth, the industrial sector had a dampening impact (Chart 2.3.1). The weak course of the industrial sector is also assessed to have been driven by the two religious holidays and bridge days in the second quarter. On the expenditures side, final domestic demand made the largest contribution to growth in annual terms. Yet, net exports continued to contribute positively to growth in this period, thus enabling a better balance among demand components. The growth in demand resulted largely from the increase in private consumption demand, whereas public sector consumption and total investments had a very limited contribution to annual growth (Chart 2.3.2). Among investment items, construction investments continued to contribute positively to growth, while machinery-equipment investments posted an annual decline for the first time since the last quarter of 2019. In the second quarter, the change in inventories had a slightly downward effect on annual growth. The positive contribution of net exports to growth continued from the first quarter into the second quarter. In this period, private consumption was the driver of quarterly growth, whereas total investments and net exports had a reducing impact. In sum, coupled with the factors such as demand which was brought forward in the first quarter and bridge days in the second quarter, GDP data for the first half of the year indicate a moderate slowdown in economic activity.

Chart 2.3.1: Annual GDP Growth and Contributions from Production Side (% Points)



Source: CBRT, TURKSTAT.

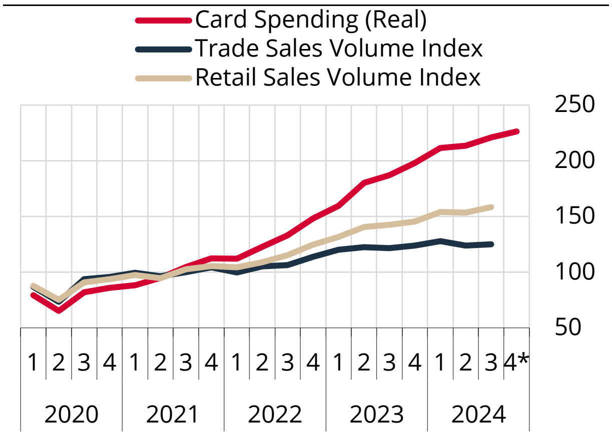
Chart 2.3.2: Annual GDP Growth and Contributions from Expenditures Side (% Points)



Source: CBRT, TURKSTAT.
* Includes changes in inventories and statistical discrepancy due to chain-linking.

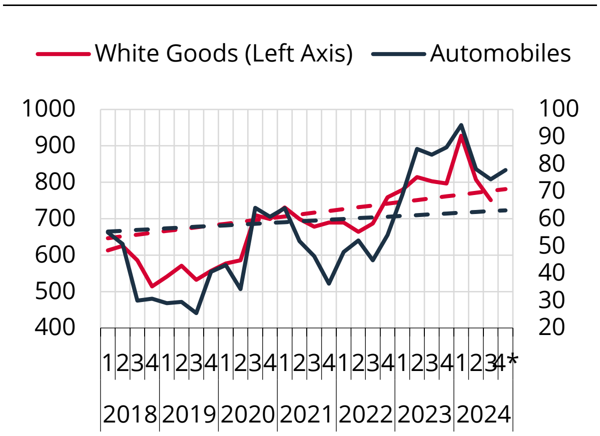
Indicators for the third quarter suggest that domestic demand continues to slow, approaching disinflation-supportive levels. In the third quarter, spending on goods excluding automobiles, which accounts for approximately half of household final consumption expenditures, increased on a quarterly basis, whereas the remaining part consisting of automobile sales and services expenditures declined. The retail sales volume index, a sub-item of the trade sales volume index, increased on a monthly and quarterly basis in August (Zoom-In 2.2). Meanwhile, among other sub-items of the trade sales volume index, trade of motor vehicles posted a monthly and quarterly increase, while wholesale trade rose month-on-month but remained flat quarter-on-quarter. The services production index, which displays movements very similar to the services expenditures component of household final consumption, decreased on a monthly basis in July and August and dropped by 0.9% on a quarterly basis (Chart 2.3.5). In the third quarter, survey data for manufacturing firms indicate a quarterly decline in domestic market orders. Information on consumption expenditures obtained from interviews with firms as of October points to a relatively flat outlook in domestic demand for the last quarter of the year (Box 2.3). Real expenditures by card remained stable in July but rose in August and September. Thus, the rise in card spending accelerated in quarterly terms (Chart 2.3.3). In card spending, it is notable that there is a shift from durable goods expenditures to semi-durable and non-durable goods expenditures. However, October data suggest a flat monthly course in card spending. Meanwhile, automobile sales increased slightly in October after a quarterly decline in the third quarter (Chart 2.3.4). White goods sales continued to decline in this period, falling to a level lower than their historical trend.

Chart 2.3.3: Consumption Indicators
(Seasonally and Calendar Adjusted, 2021=100)



Source: CBRT, TURKSTAT.
* Average of July-August retail sales volume index and trade sales volume index. As of October for card spending. Deflated by the CPI and indexed to 2021=100.

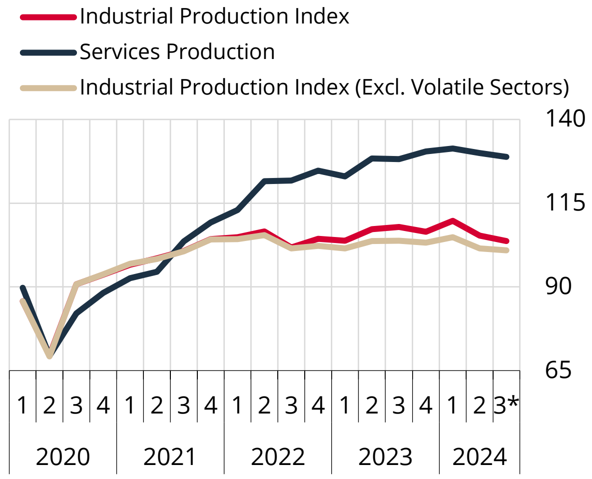
Chart 2.3.4: Sales of White Goods and Automobiles** (Thousand, Seasonally and Calendar Adjusted)



Source: CBRT, ODMD, TURKBESD.
* As of October for automobiles.
** Dashed lines show the average for the 2010-2018 period.

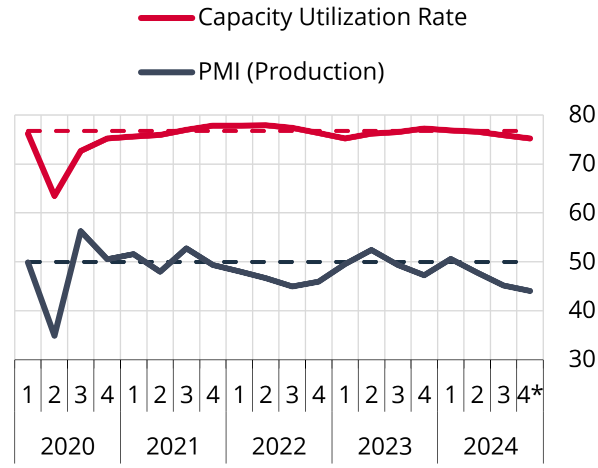
In the third quarter, both industrial and services production decreased on a quarterly basis. As of August, seasonally and calendar-adjusted industrial production fell by 1.5% quarter-on-quarter (Chart 2.3.5). When the typically highly volatile sectors are excluded, the fall in industrial production in the third quarter is assessed to be less pronounced than implied by the overall index. However, industrial production, which followed a volatile course in the second quarter of the year due to changes in the number of working days stemming from religious holidays and bridge days and contracted by 4.0% on a quarterly basis, is assessed to have fallen short of registering a recovery as of August, with the weak course across main groups persisting. Services production dropped quarter-on-quarter by 0.9% as of August. Accordingly, supply conditions were in general weaker than the demand outlook in the third quarter. Survey-based indicators such as the Business Tendency Survey (BTS) and the PMI also confirm the slowdown in industrial activity in the third quarter. In this period, survey indicators for production, employment and demand continued to decline quarter-on-quarter. The quarterly fall in the capacity utilization rate continued in the third quarter, and the capacity utilization rate dropped by 0.6 points on a quarterly basis to 75.2% as of October. Likewise, despite a limited monthly increase in October, the PMI production indicator also decreased in quarterly terms, remaining below the threshold level (Chart 2.3.6).

Chart 2.3.5: Industrial Production and Services Production Indices** (Seasonally and Calendar Adjusted, 2021=100)



Source: CBRT, TURKSTAT.
* Average of July-August.
** Industrial production excluding recorded media, computer-optical instruments, basic pharmacy and other transportation sectors that are typically volatile.

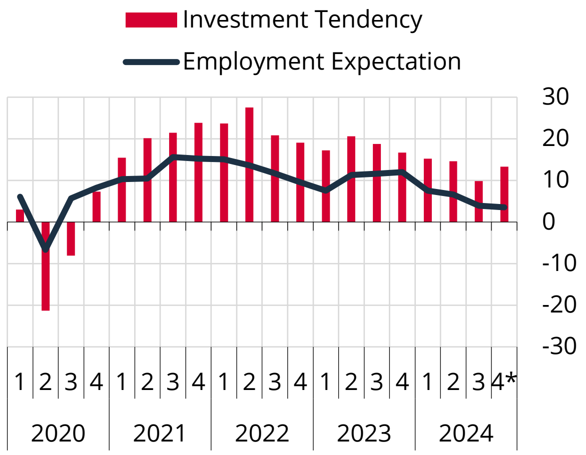
Chart 2.3.6: Capacity Utilization Rate and PMI** (Seasonally Adjusted, %)



Source: CBRT, S&P, TURKSTAT.
* As of October.
** Dashed lines show the average capacity utilization rate for the 2011-2019 period and the threshold value of 50 for the PMI.

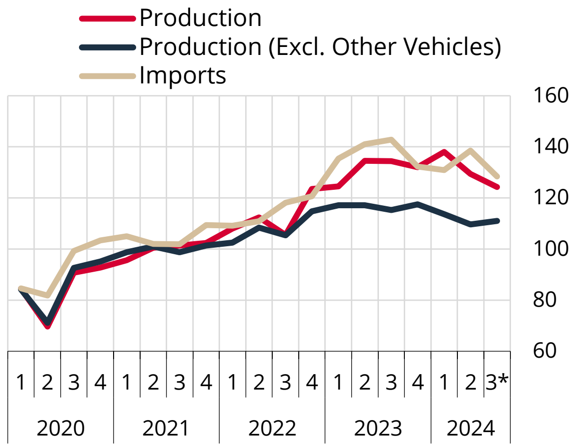
Having declined in the third quarter, investment tendencies of manufacturing industry firms increased in October, while their employment expectations remained flat (Chart 2.3.7). The production of capital goods is in line with the slowdown in investment tendencies observed in the third quarter. In the July-August period, the capital goods production index decreased on a monthly and quarterly basis, whereas the production of capital goods excluding vehicles and other transportation increased. On the other hand, imports of capital goods excluding transportation vehicles registered a monthly and quarterly decline in this period (Chart 2.3.8).

Chart 2.3.7: BTS Expectations for Fixed Capital Investment Spending and Employment (Up-Down, Seasonally Adjusted, %)



Source: CBRT.
* As of October.

Chart 2.3.8: Production and Import Quantity Indices of Capital Goods Excluding Vehicles (Seasonally Adjusted, 2015=100)

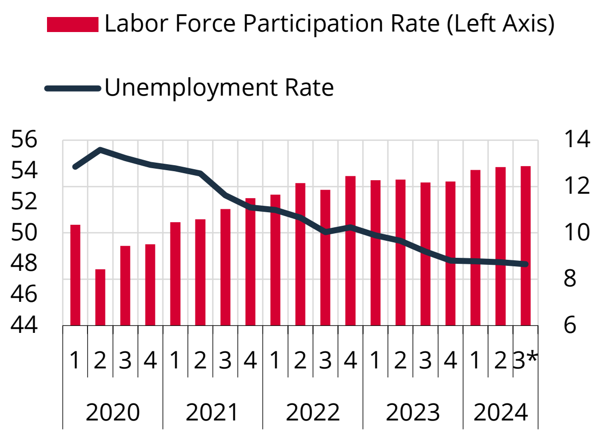


Source: CBRT, TURKSTAT.
* Average of July-August.

Labor Market Developments

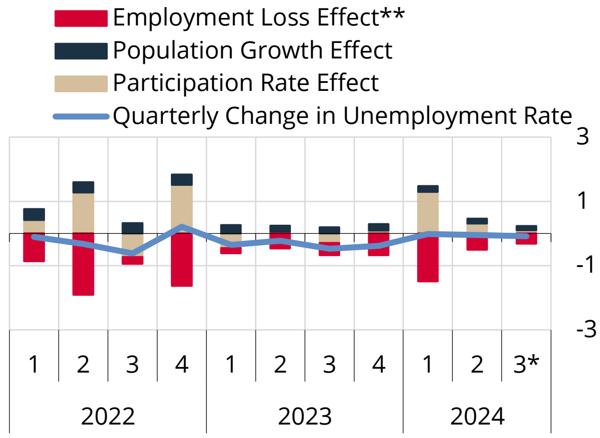
Employment continued to increase in the third quarter. In seasonally adjusted terms, employment edged up by 0.3% (113,000 people) quarter-on-quarter as of August. The seasonally adjusted labor force participation rate was up by 0.1 points to 54.3% (Chart 2.3.9). In the third quarter, the unemployment rate decreased by 0.1 points over the previous quarter to 8.6%. In this period, population growth and the increase in the participation rate had upward effects of 0.13 and 0.11 points, respectively, on the unemployment rate, while employment growth had a downward effect of 0.31 points (Charts 2.3.10 and 2.3.11). Meanwhile, given the already high level of the labor underutilization rate, a complementary indicator of the labor market, despite a quarterly decline of 0.4 points as of August, the labor market may not be as strong as implied by the main indicators.

Chart 2.3.9: Total Unemployment Rate and Labor Force Participation Rate (Seasonally Adjusted, %)



Source: TURKSTAT.
* Average of July-August.

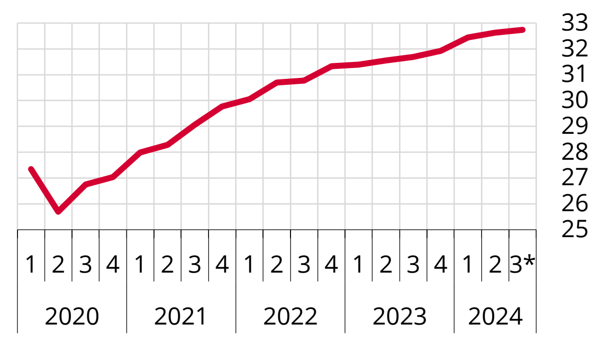
Chart 2.3.10: Contributions to Change in Total Unemployment Rate (Seasonally Adjusted, % Points)



Source: CBRT, TURKSTAT.
* Average of July-August.
** Negative value of the employment loss effect indicates an increase in employment.

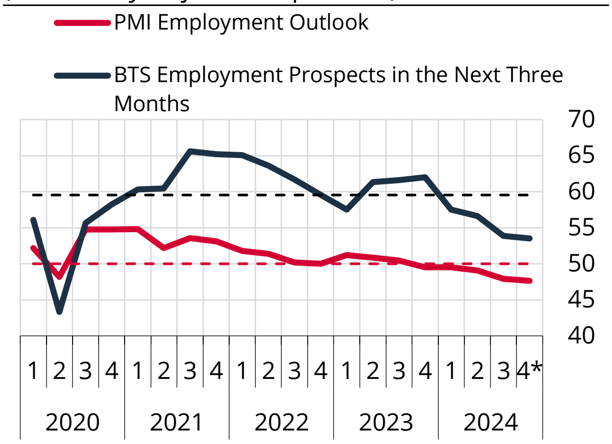
Survey indicators and high-frequency data for the third quarter suggest that the weak course of industrial employment will continue in the coming period. As of September, the total number of job listings is on the decline in quarterly terms, while the total number of job applications is on the rise. Survey data for manufacturing firms show that firms' employment outlook deteriorated on a quarterly basis in the third quarter, while employment expectations for the next three months fell below their historical average (Chart 2.3.12). On the other hand, October data point to a flat outlook in industrial employment in the last quarter.

Chart 2.3.11: Total Employment (Seasonally Adjusted, Million People)



Source: TURKSTAT.
* Average of July-August.

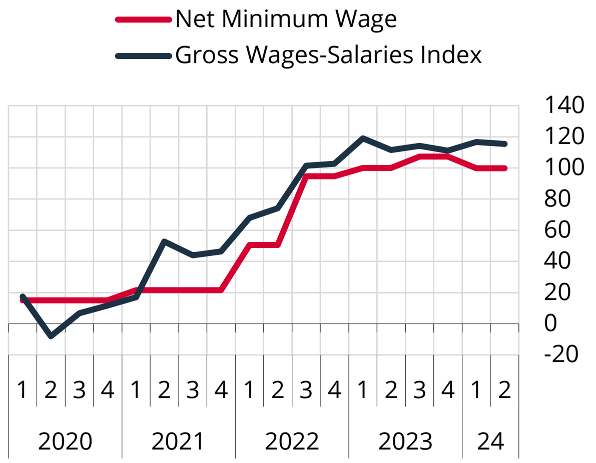
Chart 2.3.12: Employment Outlook and Expectation in the Industrial Sector** (Seasonally Adjusted, Up-Down)



Source: CBRT, S&P Global.
* As of October.
** BTS indicator is adjusted so that its neutral level will be 50 in line with the PMI. Dashed lines show the average of 2011-2019 for the BTS and the threshold value of 50 for the PMI.

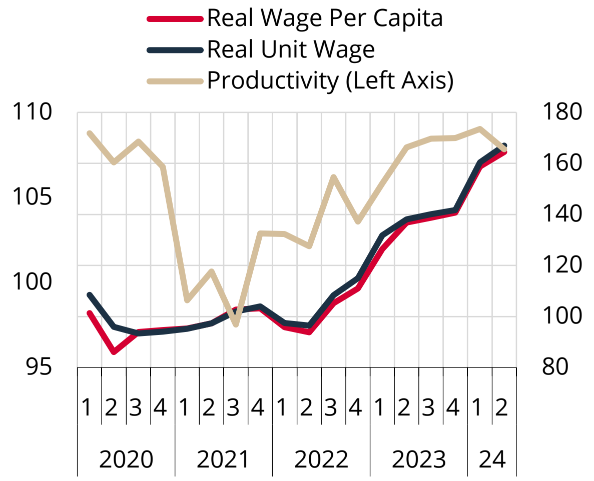
The annual rate of increase in non-farm nominal wages was 115.4% in the second quarter of 2024 (Chart 2.3.13). With the slowdown in economic activity affecting the labor market in the second quarter of 2024, partial labor productivity in the non-farm sector (non-farm value added/non-farm employment) decreased slightly. As the rise in real per capita wages continued, albeit at a slower pace, in the presence of a productivity loss, real unit wages (real per capita wage/productivity) in the non-farm sector continued to increase in the second quarter (Chart 2.3.14). However, in the rest of 2024, real unit wages are expected to follow a more moderate course compared to the previous year and contribute to the disinflation process.

Chart 2.3.13: Non-Farm Wage Index and Net Minimum Wage (Nominal, Annual % Change)



Source: CBRT, Ministry of Labor and Social Security, TURKSTAT.

Chart 2.3.14: Non-Farm Partial Labor Productivity*, Real Per Capita Wage and Real Unit Wages** (Seasonally Adjusted, 2021=100)

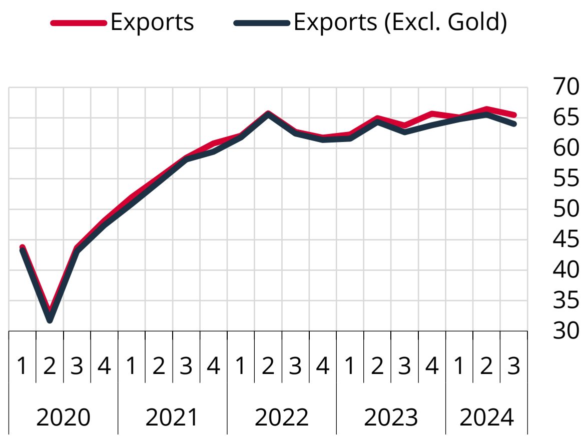


Source: CBRT, TURKSTAT.
* Non-farm value added/non-farm employment.
** Real per capita wage/productivity. Deflated by the CPI.

Foreign Trade and Balance of Payments Outlook

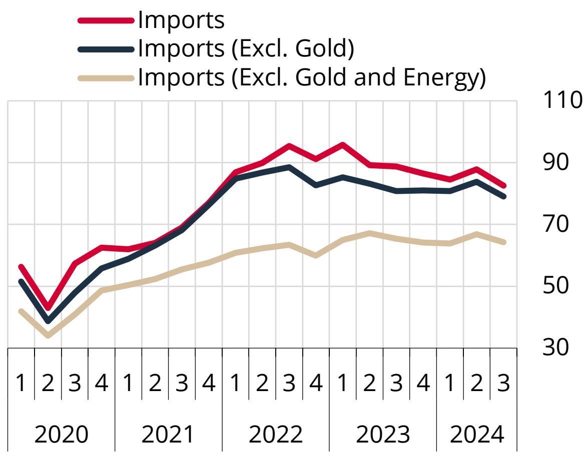
In the third quarter of 2024, exports and imports excluding gold decreased. The partial quarterly recovery in the economic activity of Türkiye's main trade partners, and the above-the-threshold level of the export climate index limited the decline in exports (Chart 2.3.15). Gold exports rose over the second quarter, whereas energy exports dropped significantly. Accordingly, seasonally and calendar-adjusted exports excluding gold and energy posted a slight decline. In this period, motor vehicles, electrical equipment, base metal and fabricated metal sectors made a positive contribution to exports, while petroleum products, other transportation vehicles and wearing apparel sectors restrained exports. In annualized terms, exports to the European Union, the Commonwealth of Independent States and African countries increased, while exports to the Middle East declined slightly. In the third quarter, seasonally and calendar-adjusted total imports declined (Chart 2.3.16). Imports of consumption and intermediate goods made the largest contribution to the quarterly decline. Gold imports fell slightly, while seasonally and calendar-adjusted energy imports recorded a more pronounced decrease. The increase in the seasonally and calendar-adjusted foreign trade deficit observed in the second quarter was replaced by a decline in the third quarter amid the fall in gold-excluded imports. In this period, both the total and the core foreign trade deficit narrowed. On the other hand, provisional foreign trade data indicate a limited monthly decrease in exports and an increase in imports in October in seasonally and calendar adjusted terms. Seasonally adjusted imports of consumption goods rose in October following the fall in the third quarter. However, this rise appears to be milder when the jewelry item classified under consumption goods is excluded. In this framework, the course of imports, particularly imports of consumption goods, in the remainder of the quarter will be closely monitored with respect to the rebalancing in demand.

Chart 2.3.15: Exports (Seasonally and Calendar Adjusted, USD Billion)



Source: CBRT, TURKSTAT.

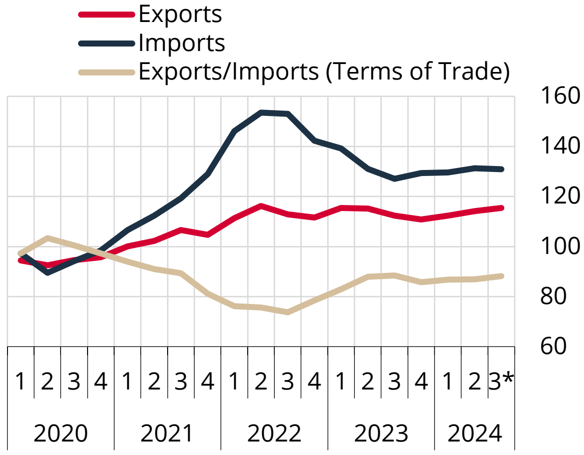
Chart 2.3.16: Imports (Seasonally and Calendar Adjusted, USD Billion)



Source: CBRT, TURKSTAT.

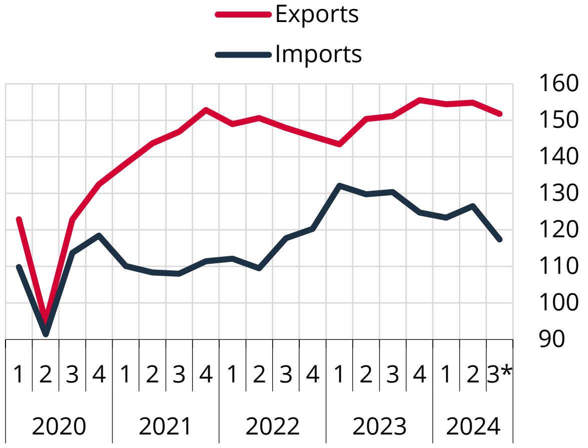
The terms of trade posted a slight increase in the third quarter, while the decline in the import quantity index outstripping the fall in the export quantity index pointed to a real rebalancing in foreign trade. According to the foreign trade unit value indices for the third quarter calculated as the July-August average, exports prices were slightly up whereas imports prices remained flat (Chart 2.3.17). Accordingly, the terms of trade continued to affect the foreign trade balance favorably in this period as well. Meanwhile, in terms of foreign trade quantity indices, seasonally and calendar-adjusted exports and imports decreased in the third quarter, with a larger decline in imports (Chart 2.3.18). Thus, the real rebalancing in foreign trade supported the improvement in the trade deficit. An analysis by goods groups reveals that all goods groups contributed to the decline in the quantity of imports, while the fall in the quantity of imports of consumption goods was stronger than that of other groups (Chart 2.3.19). The decline in July and August was influential in the course of imports of consumption goods.

Chart 2.3.17: Foreign Trade Unit Value Indices (2015=100)



Source: TURKSTAT.
* Average of July-August.

Chart 2.3.18: Foreign Trade Quantity Indices (Seasonally Adjusted, 2015=100)

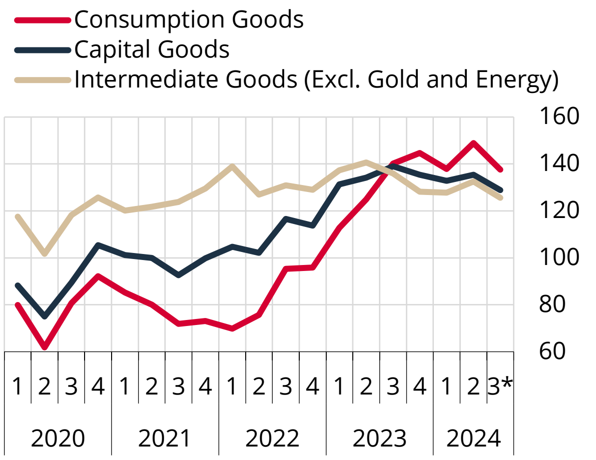


Source: CBRT, TURKSTAT.
* Average of July-August.

The services balance maintains its strong performance on the back of both travel and transportation revenues. The surplus in the balance of services continued to increase in the third quarter as seasonally and calendar adjusted balance of transportation revenues increased and net travel revenues remained high as of August (Chart 2.3.20). In addition, 2023 bulletin of the International Trade in Services Statistics, published by TURKSTAT introduced upward revisions to the services balance as of 2022. These revisions made a 12-month cumulative contribution of USD 4 billion to the services balance in July 2024 and a contribution of USD 2.2 billion since the beginning of the year. The ongoing uptrend in the seasonally and calendar-adjusted number of foreign visitors continued to contribute to the rise in travel revenues.

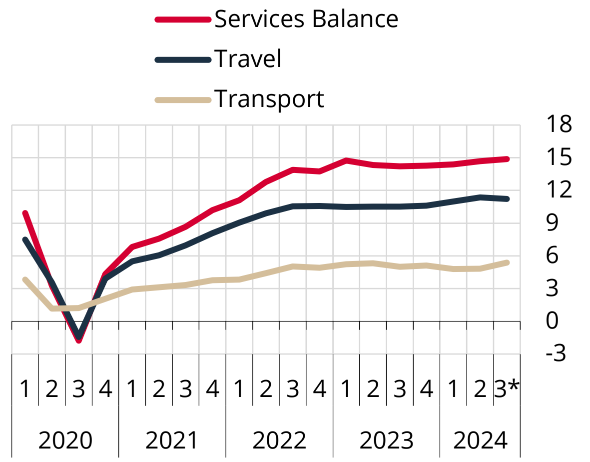
Preliminary data suggest that the number of foreign visitors also remained elevated and continued to contribute positively to net travel revenues in September.

Chart 2.3.19: Import Quantity Indices by Goods Groups (Seasonally Adjusted, 2015=100)



Source: CBRT, TURKSTAT.
* Average of July-August.

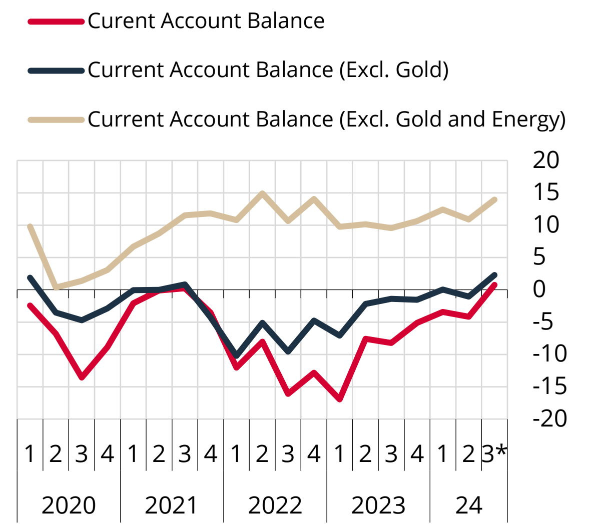
Chart 2.3.20: Services Balance (Seasonally and Calendar Adjusted, USD Billion)



Source: CBRT.
* Average of July-August.

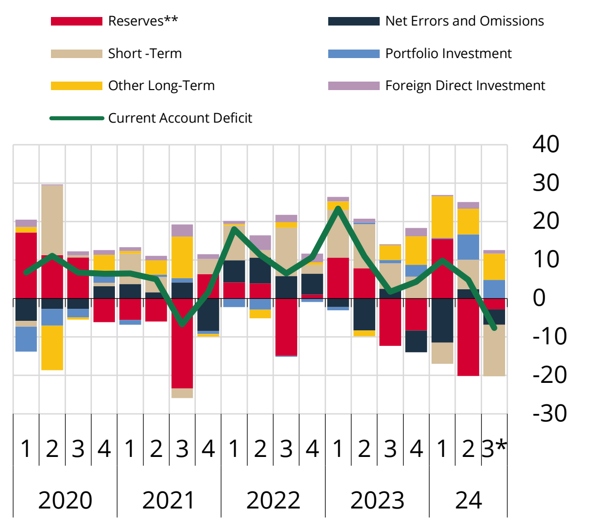
The improvement in the current account balance gained momentum in the third quarter amid the significant decline in the foreign trade deficit and the ongoing strong course of the services balance. Despite the deterioration in the primary income balance, the seasonally and calendar-adjusted current account deficit registered a marked decline in the third quarter over the previous quarter due to the significant decline in the foreign trade deficit and the continued strong contribution of the services balance (Chart 2.3.21). Similarly, the surplus in the current account balance excluding gold and energy, which is a main trend indicator, also rose in seasonally and calendar-adjusted terms in the third quarter. Both the gold and energy trade deficits decreased in this period. Besides, the revision in the services balance item had a downward effect of USD 4 billion on the 12-month cumulative current account deficit. As for the sources of the revision, the upward revision in 2023 and in the January-July 2024 period both resulted substantially from the rise in transportation revenues (freight revenues).

Chart 2.3.21: Current Account Balance (Seasonally and Calendar Adjusted, USD Billion)



Source: CBRT.
* Average of July-August.

Chart 2.3.22: Financing of the Current Account Deficit (USD Billion)



Source: CBRT.
* Cumulative of July-August.
** Denotes the CBRT reserves plus the cash and deposits at banks abroad. A negative value indicates an increase in reserves.

Portfolio investments played a smaller while long-term items played a larger role in financing the current account balance, and reserve accumulation continued, while the net errors and omissions item posted outflows. As of August, non-residents' direct investments excluding real estate decreased in the third quarter compared to the previous quarter. Meanwhile, portfolio inflows to equity and debt securities markets and inflows through short-term investment items such as loans posted a quarter-on-quarter decline (Chart 2.3.22). In the third quarter, capital inflows took place predominantly through long-term loans and the bond issuances of the banking and private sectors. In this period, the net errors and omissions item recorded outflows, while reserves increased. Leading indicators suggest that official reserves rose in September. Moreover, through the USD-denominated 10-year bond issuance of the Ministry of Treasury and Finance on September 25, amounting to USD 3.5 billion, a cash financing of USD 1.6 billion was provided, and also a liability management transaction was conducted for the first time after a long period. In this scope, the principal repayment of approximately USD 1.9 billion due until the end of 2025 was postponed to 2035.

Public Finance Developments

In the first nine months of the year, the central government budget ran a deficit of TRY 1,074.0 billion and a primary deficit of TRY 161.3 billion. In this period, the financing need was met by both domestic and external borrowing, and approximately USD 10.5 billion worth of financing was obtained from international capital markets. Thus, the external financing amount set at USD 10 billion in the Treasury Financing Program for 2024 was exceeded. It is estimated that the ratio of the central government debt stock to national income was 22.0% in September 2024, while the ratios of domestic and external debt stocks to national income were 11.1% and 10.9%, respectively. In the January-October period, the Treasury's cash deficit stood at TRY 1,703.1 billion.

In the January-September period, revenues and expenditures soared by 76.9% and 81.1%, respectively, compared to the same period of the previous year. In this period, the tax revenues-primary expenditures coverage ratio was 82.2%. The contribution of personnel expenditures to the increase in primary expenditures also stemmed from the adjustments made in civil servants' salaries. Current transfers, which have a considerable share within primary expenditures, recorded an annual increase of 68.7% in the first nine months of the year. In addition to the increase in the amount of holiday bonuses for retirees in 2024, the hike in the number of retirees due to the early retirement scheme and the high annual increase in the shares allocated from revenue also contributed to the uptick in current transfers. Moreover, a total of TRY 170.9 billion was transferred to public enterprises, including TRY 164.8 billion to the Electricity Generation Corporation as part duty losses and a total of TRY 158.2 billion to public enterprises, including TRY 71.9 billion to the Turkish Grain Board and TRY 61.7 billion to the Turkish State Railways as part of lending. On the other hand, the highest contribution to the uptick in tax revenues came from income tax. Due to the slowdown in domestic demand, the contribution of special consumption tax (SCT) and value added tax on imports to the increase in tax revenues has been declining in recent months. Corporate tax recorded a low annual increase of 37.7% in the January-September period. The total restructuring revenues of TRY 49.7 billion collected in the first nine months of the year contributed to the budget.

The annualized budget deficit to GDP ratio is estimated to be around 4.9% as of September. In the Medium-Term Program (MTP) announced in September, the 2024 realization forecasts for the ratio of expenditures and revenues to GDP are 25.4% and 20.5%, respectively, and the budget deficit-to-GDP ratio is projected to be 4.9% at the end of the year.

Zoom-in 2.2

A Close Look at the Retail Sales Volume Index

Measuring the sales of enterprises operating in the retail trade sector on a monthly basis, the retail sales volume index serves as an important leading indicator of consumption demand. Retail sales volume indices are released in a total of 12 breakdowns, 9 breakdowns at the three-digit activity level (according to NACE Rev. 2 classification) and three breakdowns at the four-digit activity level (Table 1). In this study, to understand the drivers of the recent increase in the retail sales volume index, we estimate retail sales volume indices at the four-digit NACE code level using monthly turnover data compiled from the Turkish Revenue Administration (TRA).

Table 1: Activity Groups for which Retail Sales Volume Indices Are Released

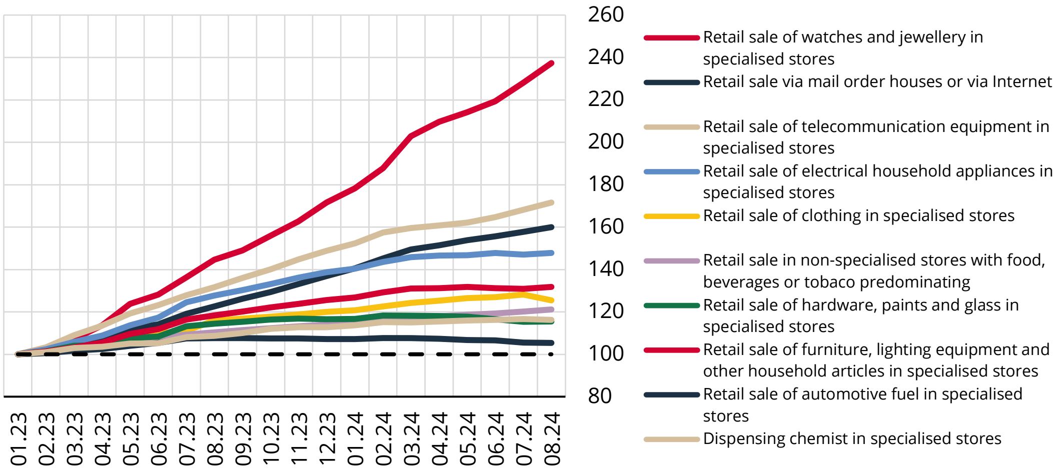
Main Group	Subgroups (NACE Rev2. Three-Digit Activity Level)
Retail Trade (G47)	G471- Retail sale in non-specialized stores
	G472- Retail sale of food, beverages and tobacco in specialized stores
	G473- Retail sale of automotive fuel in specialized stores
	G474- Retail sale of information and communication equipment in specialized stores
	G475- Retail sale of other household equipment in specialized stores
	G476- Retail sale of cultural and recreation goods in specialized stores
	G477- Retail sale of other goods in specialized stores
	G478- Retail sale via stalls and markets
	G479- Retail trade not in stores, stalls or markets
	G4711- Retail sale in non-specialized stores with food, beverages or tobacco predominating
	G4719- Other retail sale in non-specialized stores
	G4791- Retail sale via mail order houses or via Internet

Source: TURKSTAT Central Dissemination System (Biruni).

To calculate the indices, firstly, four-digit sector-level turnover indices are constructed for all retail sub-sectors using firm-level turnover data. Secondly, price indices are obtained by using three-digit sector-level turnover and volume indices released by TURKSTAT. Finally, sales volume indices are calculated by deflating the four-digit sector-level turnover indices with price indices. Since the volume indices for retail trade by mail or internet, retail trade with food, beverages or tobacco predominating and other retail trade sectors are announced by TURKSTAT at the four-digit sector level, the sales volume indices published for these sectors are used in their original forms.

Four-digit sector-level retail sales volume indices are shown in Chart 1. An analysis of the course of the calculated indices since the beginning of 2023 reveals that retail trade in watches and jewelry, retail trade by mail or internet and retail trade in telecommunication equipment have diverged from other sectors. The divergence in the retail trade in watches and jewelry sector is particularly noteworthy. This divergence was driven by the increase in retail trade in gold and gold products, which accounts for a large portion of the sector's total turnover. Sales volume indices in the retail trade of telecommunication equipment and retail trade via mail or internet sectors continue to increase in 2024, albeit at a slower pace compared to 2023. In the recent period, a moderate growth has been recorded in the retail trade with food, beverages or tobacco predominating sector, whose share in total retail turnover is relatively high at around 25%, while a flat or declining course has become evident in other sectors.

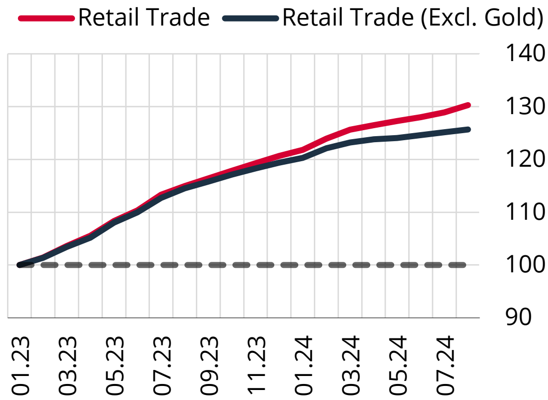
Chart 1: Retail Sale Volume Indices at Four-Digit NACE Code Level* (2023 January=100, 12-Month Moving Average)



Source: Authors' calculations, TRA, TURKSTAT.
* Sectors with a share above 2% within the domestic turnover of the retail sector in the last year are shown in the chart.

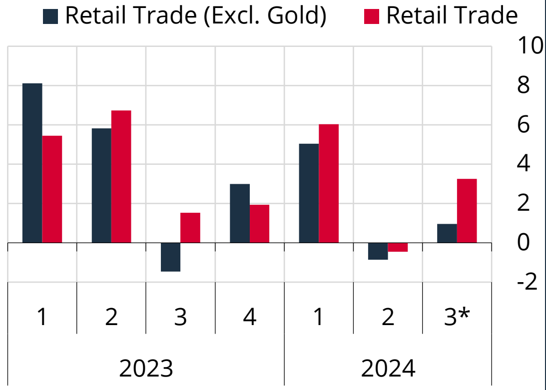
In light of these findings, the retail sales volume index excluding gold is constructed by excluding the retail sale of watch and jewelry sector from the total retail sales volume index to analyze the consumption demand trend in a more reliable way. This index has been hovering considerably below the total retail sales volume index published by TURKSTAT since June 2023 (Chart 2). Recent developments suggest that the increase in the retail sales volume index excluding gold has been milder than the rise in the total index (Chart 3). In the July-August period, the total retail sales volume index grew by 3.2% quarter-on-quarter, while the retail sales volume index excluding gold rose by 1%.

Chart 2: Retail Sales Volume Index and Retail Sales Volume Index Excluding Gold (2023 January=100, 12-Month Moving Average.)



Source: Authors' calculations, TRA, TURKSTAT.

Chart 3: Retail Sales Volume Index and Retail Sales Volume Index Excluding Gold (Seasonal and Calendar Adjusted, Quarterly % Change)



Source: Authors' calculations, TRA, TURKSTAT.
* As of July-August.

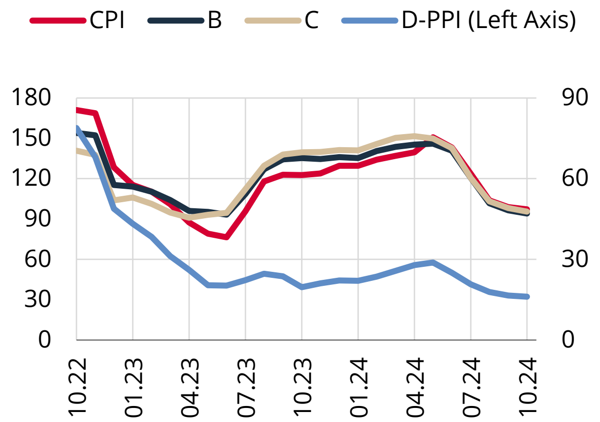
In sum, retail sales volume indices calculated at the four-digit sector level point to notable differences across sub-sectors. A significant portion of the recent increase in the retail sales volume index was driven by the watch and jewelry sector, which is mainly composed of gold and gold products. The retail sales volume index excluding this sector indicates that the uptick in consumption demand is milder.

2.4 Inflation

Consumer inflation stood at 48.6% in October 2024, decreasing by 13.2 points compared to the previous reporting period (Chart 2.4.1). The downtrend in global commodity prices that started in May extended into August, while the rise in non-energy commodity prices in September spread across all main groups in October. The global supply chain pressure index hovered close to its historical average starting from September, indicating a mild outlook in global supply constraints. The rise in currency basket grew slightly stronger in August but weakened again after September. Against this background, pressures driven by producer prices on consumer inflation eased further.

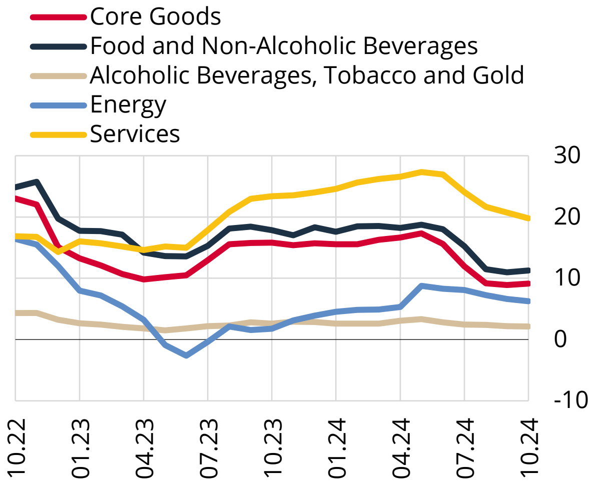
The slowdown in demand is estimated to have continued in the third quarter of 2024, approaching levels supportive of disinflation. In this period, tax revisions and price hikes in administered items with a total impact of 2.9 percentage points were among the main drivers of the inflation outlook. Notably, services inflation remained elevated, led by groups with strong time-dependent price setting and backward-indexation behavior, as well as administered items. Despite the decline in inflation expectations in this quarter, the current levels remained above the projections of the Inflation Report. An analysis of third-quarter developments by sub-items reveals that the food group made the most significant contribution to the decline in annual consumer inflation, but this pattern was disrupted in October due to prices of fresh fruits and vegetables. In this quarter, core goods and services groups also contributed to the decline, while energy and alcohol-tobacco-gold groups had a more limited downward impact on annual inflation. In October, food price hikes driven by prices of fresh fruits and vegetables came to the fore with their impact on consumer inflation (Chart 2.4.2).

Chart 2.4.1: CPI, D-PPI, B Index and C Index* (Annual % Change)



Source: TURKSTAT.
* B index: CPI excluding unprocessed food, energy, alcoholic beverages, tobacco and gold.
C index: CPI excluding food and non-alcoholic beverages, energy, alcohol-tobacco and gold.

Chart 2.4.2: Contributions to Annual CPI (% Points)

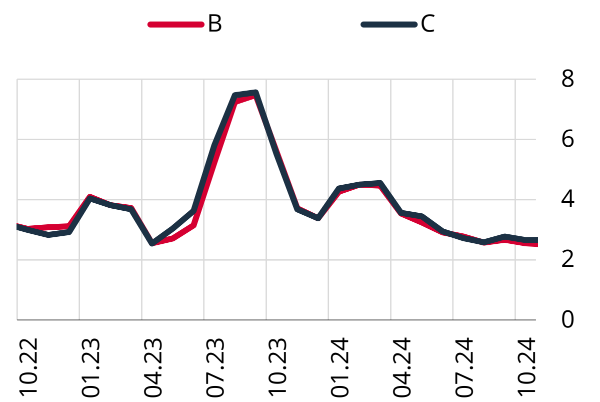


Source: CBRT, TURKSTAT.

The underlying trend of inflation decelerated, albeit remaining above projections. As of September, seasonally adjusted average quarterly increases in B and C indices were 2.7% and 2.8%, respectively, displaying a slight quarter-on-quarter slowdown (Chart 2.4.3). This was mainly driven by the adjustments in administered items and services groups with a high tendency for time-dependent price setting and backward-indexation. In October, the downtrend in B and C indicators continued. An analysis of the subgroups of the B index reveals that monthly price increases remained high in services in the third quarter but lost pace in October (Chart 2.4.4). Excluding rents, which diverge from other services items in terms of their dynamics, monthly price increases in services have gradually waned. Price increases in core goods weakened significantly in the reporting period. Although this trend was replaced by a partial increase due to the depreciation in August, core goods remained subdued in general (Chart 2.4.4). Processed food inflation, another component of the B index, also declined in this period. Alternative indicators such as median inflation, SATRIM and dynamic factor model-based (DFM) indicator displayed a similar trend, confirming the outlook in core groups. The three-month average of alternative indicators for the underlying trend fell from

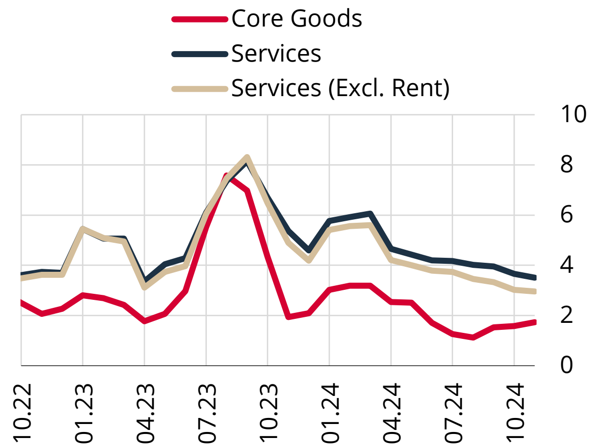
2.8% at the end of the previous quarter to 2.6% in the third quarter and to 2.4% in October (Chart2.4.5, Box 2.5). In this period, services prices posted a relatively strong increase, albeit decelerating slightly quarter-on-quarter (Table 2.4.1). The highest price increase was recorded in rents due also to the rise in the contract renewal rate in the third quarter. Rent increase rates, both in new and renewed contracts obtained from the Retail Payment System (RPS) micro data and those monitored through residential property valuation reports, remained below the current annual rent inflation in the CPI and were receding (Chart 2.4.6, Box 2.6). The lower contract renewal rate in the coming months relative to the third quarter and the decline in the reference rates in contract renewals point to a slowdown in monthly rent inflation in the last quarter of the year. In fact, monthly rent inflation decelerated in October, confirming this outlook. In the third quarter, services inflation was mostly shaped by the start of schools. Education services increased sharply on the back of university tuition fees. School bus fares and student residence fees pushed up prices of transport services and accommodation services, respectively. Adjustments in administered items, particularly the lump sum tax hike in fuel prices, had an adverse impact on transport services inflation. In this period, catering services in the restaurants-hotels group lost momentum compared to the previous quarter. Price increases in communication services were also less pronounced. Core goods prices continued to increase at a slower pace than other groups. The mild trend in prices of durable goods was mainly attributed to the course of exchange rates and the slowdown in domestic demand. Furniture prices decreased in the third quarter. After falling in the previous quarter, prices of electric and non-electric appliances (excluding white goods) remained flat in this quarter. On the other hand, quarterly inflation picked up slightly in automobiles and white goods. The uptick in automobile prices is attributed to the general safety regulation (GSR2) and the rise in the euro exchange rate in August. In October, seasonally adjusted price increases declined in both core goods and services.

Chart 2.4.3: B and C Indices (Seasonally Adjusted, Monthly % Change, Three-Month Average)



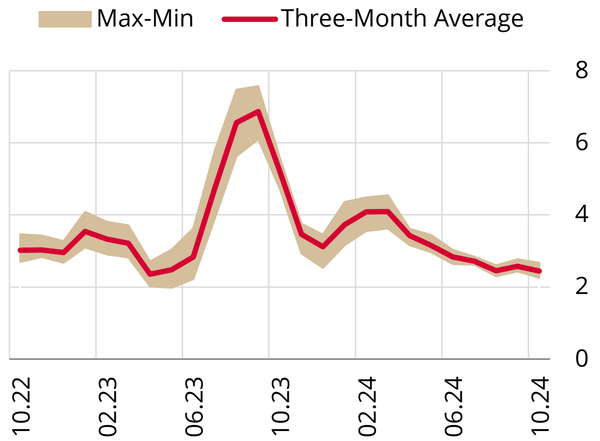
Source: CBRT, TURKSTAT.

Chart 2.4.4: Services and Core Goods Prices (Seasonally Adjusted, Monthly % Change, Three-Month Average)



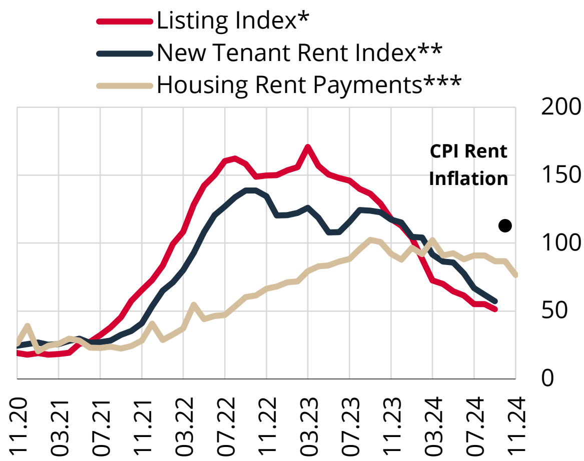
Source: CBRT, TURKSTAT.

Chart 2.4.5: Indicators of Underlying Inflation* (Seasonally Adjusted, Monthly % Change, Three-Month Average)



Source: CBRT, TURKSTAT.
* Monthly average of seasonally adjusted B and C indices and SATRIM, median inflation, exclusion of volatile items and DFM indicators. Shaded area shows the maximum and minimum range.

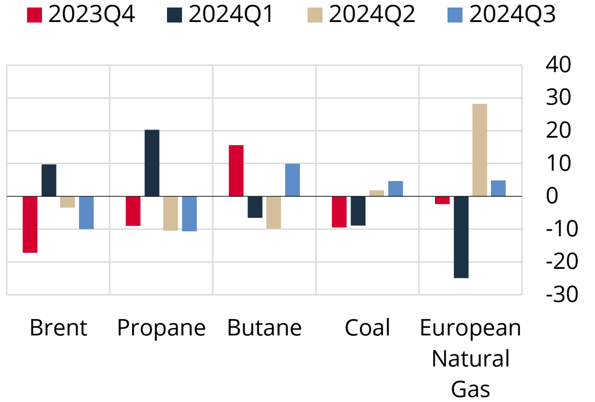
Chart 2.4.6: Leading Indicators of Rents (Annual % Change)



Source: CBRT, Sahibinden.com.
* Calculated by using the rents (TL/m2) advertised on Sahibinden.com for Türkiye's three largest cities (Istanbul, Ankara and Izmir).
** Indicator based on expert opinions obtained from mortgage loan valuation reports in the scope of the CBRT's house price index study.
*** Percentage change of new and renewed contracts compared to the previous contract including data for the first 7 days of November.

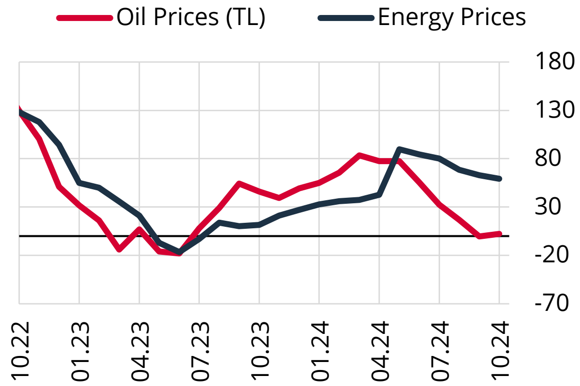
In the third quarter, domestic energy prices followed an unfavorable course. Domestic energy prices strengthened in the third quarter, increasing by 18.04% (Table 2.4.1). In this period, global energy commodity prices decreased due to Brent oil and propane prices, while prices of butane, coal and natural gas increased and diverged from this trend (Chart 2.4.7). The international Brent crude oil price, which was around USD 83 on average in June, followed a fluctuating trend due to supply-side factors and geopolitical risks despite the weak demand outlook and rose in July before falling again in the following period. The oil price, which was around USD 74 on average at the end of September, rose again in October. In this quarter, currency basket displayed a milder course following the strengthening in August. Accordingly, in this quarter, pressure from energy commodity prices weakened (Chart 2.4.8). In contrast to this outlook, energy prices in the CPI posted a sharp increase in this period due to developments in taxes and administered items. The lump-sum SCT amounts on fuel and bottled gas were revised in July. Electricity and natural gas for households were increased by 38.0%and 27.6% in July and August, respectively. Energy prices followed a mild course in September and October.

Chart 2.4.7: Energy Commodity Prices* (USD, EUR)



Source: Bloomberg.
* Brent oil prices are per barrel, coal prices are per ton, butane and propane prices are per gallon. European natural gas prices are in euro and per MWh.

Chart 2.4.8: Energy Prices (Annual % Change)



Source: Bloomberg, TURKSTAT.

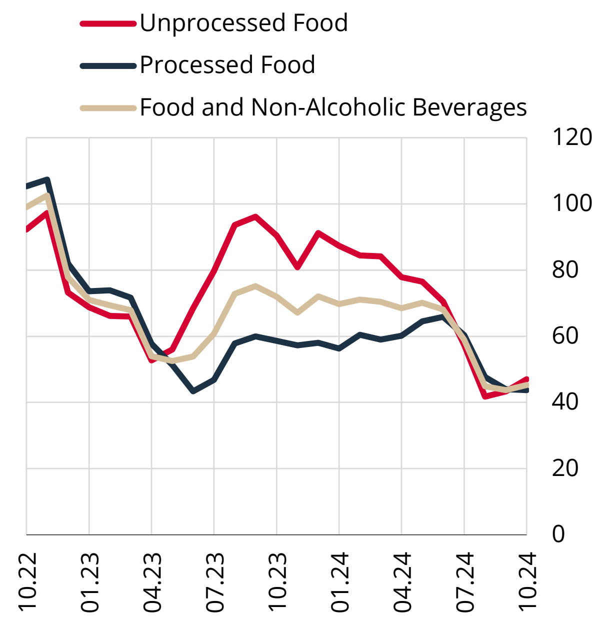
Table 2.4.1: Consumer Prices

	Quarterly % Change (Seasonally Adjusted)				Annual % Change			
	2023	2024			2023	2024		
	IV	I	II	III	IV	I	II	III
CPI	**11.12**	**13.03**	**8.90**	**9.32**	**64.77**	**68.50**	**71.60**	**49.38**
B	**10.46**	**13.96**	**8.97**	**8.21**	**68.02**	**71.89**	**70.40**	**48.23**
C	**10.45**	**14.25**	**9.07**	**8.55**	**70.64**	**75.21**	**71.41**	**49.10**
1. Goods	9.74	10.65	7.16	8.00	55.46	58.17	62.56	40.27
Energy	**17.08**	**10.80**	**6.41**	**18.04**	**27.19**	**37.32**	**84.58**	**62.94**
Food and Non- Alcoholic Beverages	**10.51**	**12.23**	**8.89**	**6.50**	**72.01**	**70.41**	**68.08**	**43.72**
Unprocessed Food	10.51	11.71	9.36	6.34	91.23	84.14	70.50	43.34
Fresh Fruits and Vegetables	2.96	6.97	18.26	2.41	81.29	82.67	78.61	32.70
Other Unprocessed Food	15.36	14.66	4.19	8.93	97.47	85.02	66.30	50.07
Processed Food	10.50	12.68	8.48	6.64	58.05	58.97	65.89	44.05
Bread and Cereals	7.26	11.98	11.09	7.04	58.42	58.80	71.15	42.83
Other Processed Food	12.17	13.01	7.28	6.45	57.88	59.02	63.43	44.77
Goods (Excl. Energy and Food)	6.77	9.50	6.16	5.90	**55.00**	**57.59**	**52.56**	**31.00**
Core Goods	**6.37**	**9.89**	**5.23**	**4.67**	**52.81**	**56.46**	**50.62**	**28.26**
Clothing and Footwear	8.02	8.60	6.64	5.35	39.74	49.12	46.87	29.93
Durable Goods (Excl. Gold)	3.89	9.61	3.69	3.98	60.70	61.11	46.89	22.77
Other Core Goods	9.17	11.31	6.76	5.30	50.42	55.25	59.17	36.60
Alcoholic Beverages, Tobacco	**9.28**	**5.42**	**14.84**	**15.16**	**71.26**	**62.98**	**67.93**	**52.35**
Gold	**10.84**	**16.07**	**2.41**	**11.22**	**70.59**	**84.78**	**59.22**	**46.54**
2. Services	**14.41**	**19.20**	**13.11**	**12.34**	**90.66**	**96.48**	**95.27**	**72.92**
Rent	20.63	26.09	18.68	20.36	108.58	123.95	123.64	117.43
Restaurants and Hotels	12.57	20.02	11.38	9.83	93.24	94.97	90.67	65.41
Transport	12.88	12.64	12.24	8.30	92.44	94.41	103.54	53.92
Communication	12.83	16.00	11.31	6.45	63.92	71.99	67.45	55.08
Other Services	13.62	17.65	12.12	12.26	85.20	90.41	89.06	68.49

Source: TURKSTAT.

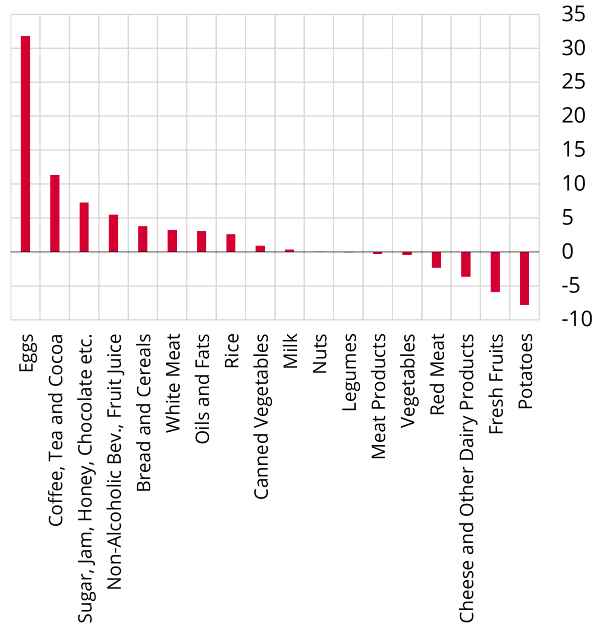
Annual food inflation, which fell below the headline inflation in April, maintained this level throughout the third quarter, but prices rose sharply in October due to fresh fruits and vegetables. Annual inflation in food and non-alcoholic beverages decreased by 24.36 points to 43.72% in the third quarter. Annual inflation fell by 27.16 points in unprocessed food and 21.84 points in processed food (Chart 2.4.9). In seasonally adjusted terms, food inflation decelerated quarter-on-quarter. In this quarter, quarterly inflation in fresh fruits and vegetables weakened quite significantly (2.41%), while quarterly inflation in other food groups remained elevated with a limited increase (Table 2.4.1). In the third quarter, the rise in the prices of fresh fruits and vegetables was significantly below their historical averages, more notably in fruits (Chart 2.4.10). In the other food group, egg prices, which had posted a rise below their historical average in the second quarter, stood out with a high rate of increase in this quarter. Eggs were followed by the tea group due to price hikes by ÇAYKUR in July and September in response to the increase in fresh tea purchasing prices, while prices of confectionery and chocolates were other products that posted high rates of increase. White meat prices rose above their historical average due to fish prices, while red meat prices remained below their historical trend. Other products that remained below their historical price averages in the third quarter were cheese, other dairy products and potatoes (Chart 2.4.10). In October, unprocessed food prices posted a strong increase driven by fresh fruits and vegetables due to the seasonal field-greenhouse transition, while prices of foods excluding fresh fruits and vegetables posted a moderate increase.

Chart 2.4.9: Food Prices (Annual % Change)



Source: TURKSTAT.

Chart 2.4.10: Food Prices by Sub-Items* (2024Q3 % Deviation of Change from Historical Average, Ranked)



Source: CBRT, TURKSTAT.
* On the basis of food sub-items, the difference between the 2024Q3 quarterly percentage change and the historical average (third quarter average of the 2012-2021 period).

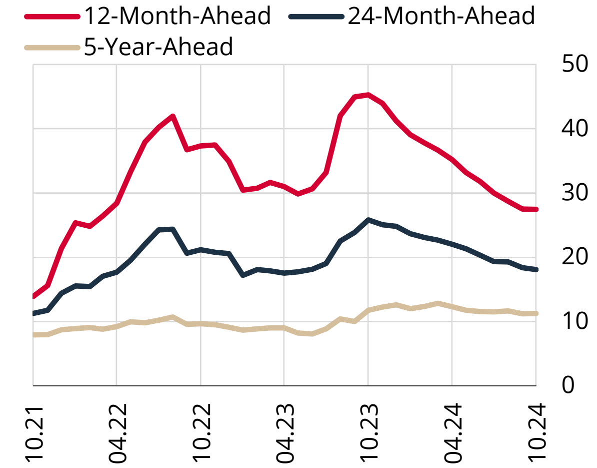
In the third quarter of the year, prices of alcoholic beverages and tobacco products increased by 15.16%. In July, lump-sum tax on alcohol and tobacco products was increased in proportion to the D-PPI. In September, firm-driven price hikes were observed in tobacco products. In the third quarter, prices of alcoholic beverages increased by 17.45%, while prices of tobacco products rose by 14.96%. Annual inflation in the alcoholic beverages and tobacco group dropped by 15.57 points quarter-on-quarter to 52.35%, and the contribution of the alcohol-tobacco group to annual inflation decreased by 0.54 points in this quarter.

Drivers of Inflation

Inflation expectations mostly maintained their downtrend, yet remained above the projections in the previous Inflation Report. According to the Survey of Market Participants in October, the 12-month-ahead inflation expectation decreased by 2.58 points to 27.44%, while the 24-month-ahead inflation expectation fell by 1.24 points to 18.08%. The five-year-ahead inflation expectation was revised downwards by 0.23

points to 11.27% (Chart 2.4.11). Meanwhile, inflation expectations for end-2024 and end-2025 increased slightly after July and stood at 44.11% and 25.64%, respectively, in October, remaining above the forecast range presented in the previous Inflation Report. Although inflation expectations for the end of the current year hovered above the forecasts, both the 12-month-ahead expectations and those for the end of next year indicate that the disinflation process will be maintained and the forecasts that function as intermediate targets will be achieved with a delay. An analysis of household and real sector expectations reveals divergences. Both the BTS, which measures the expectations of the real sector, and the Consumer Tendency Survey show a decline in inflation expectations, but the gaps with the Survey of Market Participants have narrowed slightly. When data from different sources are analyzed, it is observed that expectations continue to improve, albeit at a slower pace than envisaged. On a quarterly basis, the diffusion index posted a quarter-on-quarter decline (Chart 2.4.12). The services sector continued to push the diffusion index upwards in the third quarter. In addition, adjustments in tariffs in administered energy items had a negative impact on firms' price setting behavior and limited the decline in the diffusion index.

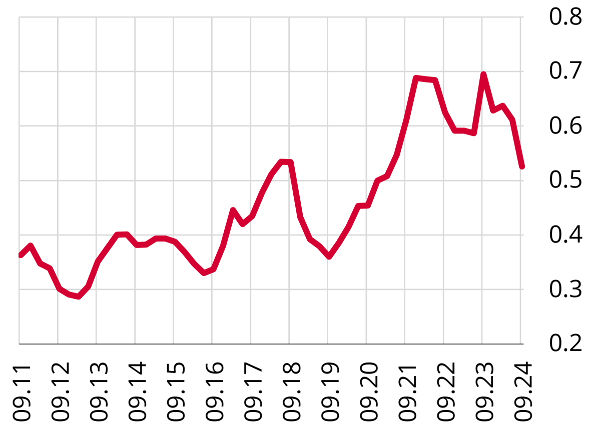
Chart 2.4.11: Consumer Inflation Expectations* (%)



Source: CBRT.

* Results of the CBRT Survey of Market Participants that polls real and financial sector representatives as well as professionals.

Chart 2.4.12: CPI Diffusion Index* (Seasonally Adjusted, Quarterly Average)

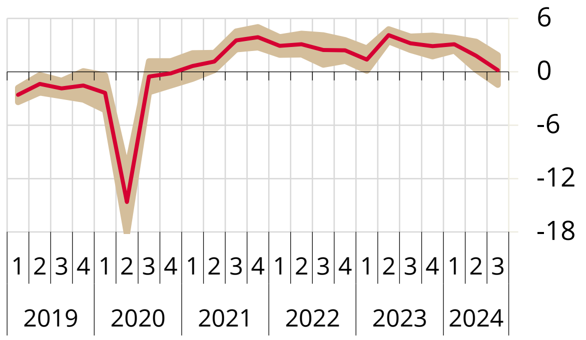


Source: CBRT, TURKSTAT.

* Calculated as the ratio of the difference between the number of items with increasing prices and the number of items with decreasing prices to the total number of items.

Aggregate demand continues to slow down, approaching levels supportive of disinflation. The slowdown in aggregate demand conditions that started in the second quarter is expected to continue in the third quarter as well. While the baseline output gap estimation is significantly closer to the neutral level, the slightly wider uncertainty band indicates that the divergence between series calculated by using different methods and based on different data sources has increased (Chart 2.4.13). In line with this, industrial production and services production declined quarter-on-quarter in the third quarter (Chart 2.3.5), while demand indicators such as retail sales volume and credit card spending posted a slight quarterly increase (Chart 2.3.3). An analysis of real credit developments based on 13-week moving averages reveals that total credit use (adjusted for exchange rate effects) did not display a significant change in the last quarter in accordance with macroprudential measures (Chart 2.4.14). In the previous reporting period, the limited slowdown in corporate loans was largely offset by the moderate increase in retail loan use. While the rise in credit card expenditures stood out in retail loans, housing loans also displayed a partial pickup.

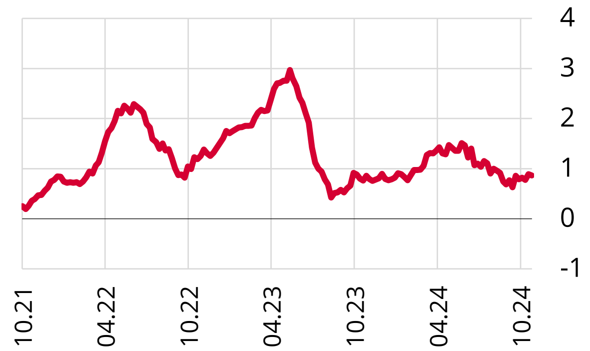
Chart 2.4.13: Output Gap* (%)



Source: CBRT.

* Displayed with 95% confidence interval, which is computed based on eight output gap indicators calculated with various methods.

Chart 2.4.14: Total Credit Change* (13-Week Average, FX-Adjusted, Real, Standardized Value)

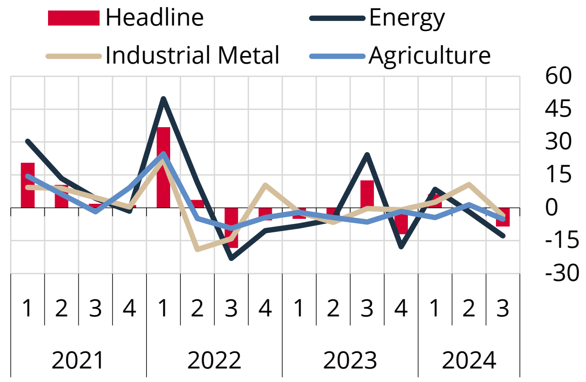


Source: CBRT.

* Weekly credit changes adjusted for exchange rates are deflated by the CPI. The 13-week average is taken after weekly real changes are standardized. The mean and standard deviations of the series are calculated based on the 2006-2019 period.

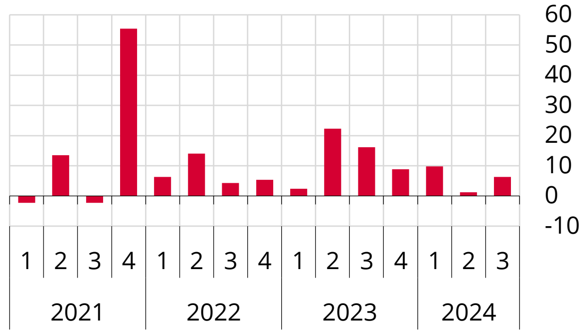
In the third quarter of the year, global commodity prices declined, while the rise in the basket exchange rate strengthened slightly. In August, commodity prices declined across all groups. In September, energy prices declined significantly, while industrial metal and agricultural prices increased. On a quarterly basis, the overall commodity index declined (Chart 2.4.15). On the other hand, in October, strong price increases were observed across all main groups, with the energy group displaying a more apparent increase. The currency basket, which remained almost flat in the second quarter, increased moderately in the third quarter (Chart 2.4.16). The depreciation in the Turkish lira played a role in the acceleration of price increases in the energy group as well as in durable goods items with high exchange rate sensitivity such as automobiles and white goods.

Chart 2.4.15: Commodity Price Indices (Quarterly % Change)



Source: Goldman Sachs.

Chart 2.4.16: Currency Basket* (Quarterly % Change)

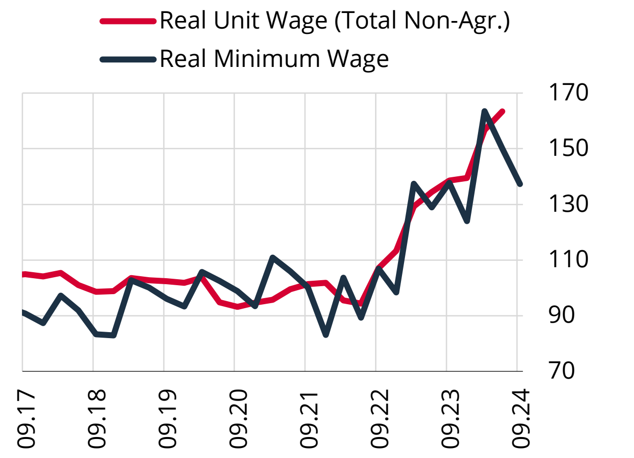


Source: CBRT.

* USD and euro have equal weights. Calculations are based on the average exchange rate in the last month of the relevant quarter.

The underlying producer inflation remained moderate. In the second quarter, the rise in real unit wages was more limited compared to the first quarter (Chart 2.4.17). As the minimum wage, which is an important benchmark for wages across the economy, was raised only in January this year, real wages are expected to decline in the second half of the year, even if nominal wage increases continue. An analysis of transportation costs reveals that global and Chinese container indices declined in the third quarter, while dry cargo transportation indices fluctuated on a month-to-month basis but remained almost flat in the second half of the year. In the same period, commodity prices declined, while global supply chain conditions edged up slightly and converged to their historical averages. In sum, global cost conditions remained favorable in the third quarter. On the other hand, the moderate rise in exchange rates in the third quarter slightly increased cost pressures in terms of Turkish lira. Reflecting these cost factors, both producer inflation and underlying manufacturing inflation remained moderate in the previous reporting period (Chart 2.4.18). The annualized underlying manufacturing inflation stood at 19.7% in October, significantly below the current annual producer inflation (32.2%).

Chart 2.4.17: Real Unit Wage per Hour Worked* (Value Added, 2021=100, Seasonally Adjusted) **and Real Minimum Wage**** (2021=100)



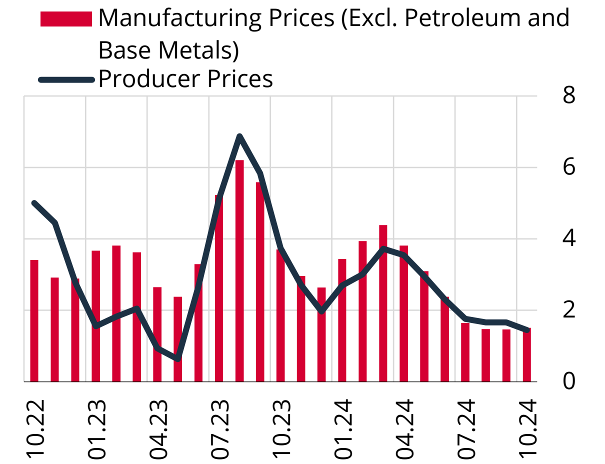
Source: CBRT, TURKSTAT.

* Deflated by the CPI. Real wage per hour worked/productivity.

** Deflated by the seasonally adjusted CPI.

Forecast is used for the 2024Q3 inflation data.

Chart 2.4.18: Manufacturing Prices Excluding Petroleum and Base Metals (Monthly % Change, Three-Month Moving Average)



Source: CBRT, TURKSTAT.

The impact of taxes and administered items on headline inflation increased in the third quarter. Tariffs for household electricity and natural gas were raised significantly in July and in August, respectively. The rise in commercial electricity tariffs and natural gas tariffs in first-tier industrial[2] and electricity producers had an indirect adverse impact on consumer inflation through the cost channel. Automatic tax revisions in fuel oil based on the D-PPI and the increases in electricity prices led to tariff hikes in various transportation services. The rise in bridge and highway tolls in August was another factor that had an adverse impact on inflation through the expectations channel, albeit with limited direct effects. With the start of the new academic year, student contribution fees and public dormitory fees were raised to compensate for the past high inflation. In the food group, tea prices were affected by ÇAYKUR's price hike in September. Prices of tobacco products, which posted price hikes in July and August due to the lump sum tax revision, increased in September due to the producer companies. Meanwhile, the tax structure of tobacco products was changed in September, and the fiscal multiplier was reduced by lowering the ad valorem SCT rate. As the lump-sum SCT amount was not raised as much as to compensate for the tax revenue loss stemming from the decrease in the ad valorem SCT rate, the overall impact limited firm-driven cost pressures. Unlike previous years, the declines in the fiscal multiplier had a smaller weakening impact on inflation inertia due to the high level of lump-sum SCT coupled with the fact that lump-sum amounts were increased in January and July by the same amount as the producer inflation in the previous six months. The revision in the reference euro rate for medicine prices in late October was another important development that took place in administered prices in the previous reporting period. Half of the impact of this adjustment was reflected in October inflation.

[2] Tier 1: Free consumers with an annual consumption of 300.000 sm^3 or less.